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IN THE

Supreme Court Of The United States

October Term, 1996

United Companies Lending Corporation,
Petitioner,

v.

Michael D. McGehee, and Joyce McGehee,
Respondents.

On Petition for a Writ of Certiorari to the
Supreme Court of Alabama

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

I. Does the Supremacy Clause of the United States Constitution require state courts to give the same degree of deference to a federal administrative agency's regulations and interpretations as is required of a federal court?

II. Where a state statute incorporates a federal administrative agency's regulations as part of a state regulatory standard:

A. Does an erroneous interpretation of the incorporated federal regulation, based upon a state court's failing to defer to the federal administrative agency's interpretation, require reversal as a matter of federal law; and

B. Where the erroneous interpretation of federal regulations could not have been foreseen under any reasonable interpretation of the regulation does the state court's decision violate a person's right to due process?

LIST OF UNITED COMPANIES LENDING CORPORATION'S PARENT COMPANIES AND SUBSIDIARIES

The parent company of petitioner is United Companies Financial Corporation. United Companies Lending Corporation has no subsidiaries.

TABLE OF CONTENTS

QUESTIONS PRESENTED i

LIST OF UNITED COMPANIES LENDING CORPORATION'S PARENT COMPANIES AND SUBSIDIARIES ii

TABLE OF AUTHORITIES v

OPINIONS BELOW 1

JURISDICTION 2

CONSTITUTIONAL PROVISIONS, STATUTES AND REGULATIONS INVOLVED 2

STATEMENT 3

REASONS FOR GRANTING THE PETITION 9

I. Federal Courts Must Defer to Federal Agency Regulations and Agency Interpretations 10

II. Federal Agency Regulations and Interpretations are Federal Law for Purposes of the Supremacy Clause 11

III. A State Court's Erroneous Interpretation of Federal Regulations is an Issue of Federal Law 13

IV. The Alabama Supreme Court's Failure to Defer to HUD Regulations and Interpretations Caused it to Misinterpret Federal Regulations and to Violate United's Due Process Rights 15

A. The Alabama Supreme Court's Failure to Defer to HUD Regulations and Interpretations Led it to Err 15

B. The Alabama Supreme Court Violated United's Rights to Due Process Under Law 17

V. The Questions Presented Are Important 19

CONCLUSION 22

APPENDIX A Mobile Circuit Court's Opinion (Dated May 11, 1995) A-1

APPENDIX B Alabama Supreme Court's Original Opinion (Dated March 22,1996) B-1

APPENDIX C Alabama Supreme Court's Opinion on McGehee's Petition for Rehearing (Dated October 11, 1996) C-1

APPENDIX D Alabama Supreme Court's Order Denying United's Application for Rehearing (Dated December 6, 1996) D-1

APPENDIX E Alabama Code Sections 5-19-4(g) and 5-19-31(a) E-1

APPENDIX F 24 C.F.R. Sections 202.10 through 202.14 ..... F-1

APPENDIX G. Exhibits C and K to United Companies Lending Corporations's Application for Rehearing and Brief in Support of Application for Rehearing G-1

TABLE OF AUTHORITIES

CASES **PAGE(S)**

Adams v. Robertson, 65 U.S.L.W. 4180 (March 3, 1997).....9

American Hosp. Ass'n v. Bowen, 834 F.2d 1037, 1045 (D.C. Cir. 1987).....3

American Surety Co. v. Baldwin, 287 U.S. 156. 164 (1932).....9

BMW of North America, Inc. v. Gore, 116 S. Ct. 1589 (1996).....17

Blum v. Bacon, 457 U.S. 132 (1982).....12

Bouie v. City of Columbia, 378 U.S. 347 (1963).....17

Brannan v. United Student Aid Funds, Inc., 94 F.3d 1260 (9th Cir. 1996).....12

Brubaker v. Morton, 500 F.2d 200 (9th Cir. 1974).....8

Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc., 467 U.S. 837 (1984).....3, 11

Chrysler Corp. v. Brown, 441 U.S. 281 (1979).....3, 12

City of New York v. F.C.C., 486 U.S. 57 (1988).....11, 12

Delorme v. North Dakota Department of Human Services, 492 N.W.2d 585 (N.D. 1992).....12

District of Columbia Court of Appeals v. Feldman, 460 U.S. 462, 482 (1983).....19

Farmer v. Hypo Holdings, Inc., 1995 WL 664589 (Ala. Nov. 9, 1995) (opinion withdrawn and superseded on rehearing).....4

Farmer v. Hypo Holdings, Inc., 675 So. 2d 387 (Ala. 1996).....19

Good Samaritan Hospital v. Shalala, 508 U.S. 402 (1993).....11

Ideal Federal Savings Bank v. Murphy, 663 A.2d 1272 (Md. 1995).....13

Lynnbrook Farms v. Smithkline Beecham Corp., 79 F.3d 620 (7th Cir. 1996).....11

CASES **PAGE(S)**

Matarazzo v. Rowe, Commissioner of Income Maintenance, 623 A.2d 470 (Conn. 1993).....13
Michigan v. Long, 463 U.S. 1032 (1983).....14
Pennsylvania v. Labron, 116 S. Ct. 2488 (1996).....14
Rooker v. Fidelity Trust Co., 263 U.S. 413, 416 (1923)..19-20
Samara Development Corp. v. Marlow, 556 So. 2d 1097 (Fl. 1990).....13
Shalala v. Guernsey Memorial Hospital, 115 S. Ct. 1232 (1995).....12
Standard Oil Co. of California v. Johnson, 316 U.S. 481 (1942).....13, 14
Saunders v. Shaw, 144 U.S. 317 (1916).....9
Thomas Jefferson University v. Shalala, 512 U.S. 504, 114 S. Ct. 2381 (1994).....11
Thorpe v. Housing Authority of Durham, 393 U.S. 268 (1969).....8
Three Affiliated Tribes of the Fort Berthold Reservation v. Wold Engineering, P.C., 467 U.S. 138 (1984).....13, 14
Totemoff v. State of Alaska, 905 P.2d 954, 967 (Alaska 1995).....13
Udall v. Tallman, 380 U.S. 1 (1965).....8
United States v. Harris, 347 U.S. 612 (1954).....17

STATUTES AND REGULATIONS

U.S. Const. Art. VI, cl. 2.....2
U.S. Const. Amend. XIV, § 1.....2
The National Housing Act 12 U.S.C. § 1701 to 1750g.....4
5 U.S.C. § 553 (1994).....3
12 U.S.C. § 1715(b).....4
28 U.S.C. § 1257(a).....2
42 U.S.C. § 3535(d).....4
24 C.F.R. Part 202.....2
24 C.F.R. §§ 202.10-202.14.....2
24 C.F.R. § 202.11(a).....4

STATUTES AND REGULATIONS **PAGE(S)**

24 C.F.R. § 202.11(a)(1) 5
24 C.F.R. § 202.12(m) 6, 8
24 C.F.R. § 202.14 5
24 C.F.R. § 203 5
24 C.F.R. § 203.4 5
61 Fed. Reg. 2650 (1996) 6
61 Fed. Reg. 36452 (1996) 6
Ala. Code § 5-19-4(g) 2, 4, 6, 7
Ala. Code § 5-19-31(a) 2, 4, 6, 7, 8

MISCELLANEOUS

Franklin D. Cordell, Note, The Private Mortgage Insurers Action for Rescission for Misrepresentation: Limiting a Potential Threat to Private Sector Participation in the Secondary Mortgage Market, 47 WASH. & LEE L. REV. 587,587-94 (Summer 1990) 21

Jo Anne Bradner, The Secondary Mortgage Market and State Regulation of Real Estate Financing, 36 EMORY L.J. 971, 973-82 (Summer 1987) 21

Robin Paul Malloy, The Secondary Mortgage Market A Catalyst for Change in Real Estate Transactions, 39 SW. L.J. 991, 991-1001, 1013-18 (February, 1986) 21

No. ____

IN THE

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October Term, 1996

United Companies Lending Corporation,
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v.

Michael D. McGehee, and Joyce McGehee,
Respondents.

On Petition for a Writ of Certiorari to the
Supreme Court of Alabama

PETITION FOR A WRIT OF CERTIORARI

United Companies Lending Corporation ("United") petitions for a writ of certiorari to review the judgment of the Supreme Court of the State of Alabama.

OPINIONS BELOW

The Alabama Supreme Court's opinion, dated October 11, 1996, (App., C-1 to C-28), which withdrew and replaced the court's prior opinion, is not yet released for official publication, but may be found at 1996 WL 583767. The Alabama Supreme Court's order, dated December 6, 1996, (App., D-1), denying United's petition for rehearing, is unreported. The court's initial opinion, dated March 22, 1996, (App., B-1 to B-8), reversing the trial court's order, is unreported. The trial court's order on cross motions for summary judgment, dated May 11, 1995, (App., A-1 to A-9) is unreported.

JURISDICTION

The judgment of the Supreme Court of Alabama was entered on October 11, 1996. The court denied United's timely motion for rehearing on December 6, 1996. This Court's jurisdiction is invoked pursuant to 28 U.S.C. § 1257(a).

CONSTITUTIONAL PROVISIONS, STATUTES AND REGULATIONS INVOLVED

The Supremacy Clause of the United States Constitution provides, "[t]his Constitution, and the laws of the United States which shall be made in pursuance thereof; and all treaties made, or which shall be made, under the authority of the United States, shall be the supreme law of the land; and the judges in every state shall be bound thereby, any thing in the constitution or laws of any state to the contrary notwithstanding." U.S. Const. Art. VI, cl. 2.

The Due Process Clause of the Fourteenth Amendment to the Constitution provides that "nor shall any state deprive any person of life, liberty, or property, without due process of law." U.S. Const. amend. XIV, § 1.

Alabama's Consumer Credit Act provides a 5% limit on "points" charged in connection with certain loans. Ala. Code § 5-19-4(g) (1994). App., E-1. Section 5-19-31(a) provides that certain restrictions of the Consumer Credit Act, including the points limitation "shall not apply to any loan ... or other transaction involving an interest in real property or the sale, lease, or mortgage of an interest in real property, where the creditor is a lending institution which is an approved mortgagee under the provisions of the National Housing Act." Ala. Code § 5-19-31(a) (1994). App., E-1 to E-2.

The Secretary for the Department of Housing and Urban Development ("HUD") has promulgated certain regulations implementing the National Housing Act. *See generally* 24 C.F.R. Part 202 (1994). The specific regulations implicated in this petition are 24 C.F.R. §§ 202.10-202.14, which govern the approval of mortgagees under the National Housing Act.

App., F-1 to F-14. HUD has issued an official letter interpreting those regulations. App., G-1 to G-4.

STATEMENT

This case involves a state court's misinterpretation of regulations promulgated by HUD governing the manner in which an institution may be approved as a mortgagee to participate in the mortgage insurance programs authorized under the National Housing Act ("National Housing Act"). The question presented is whether a state court violates the Supremacy Clause when it fails to defer to a federal agency's regulations and interpretations on a question of federal law. Under this Court's decision in *Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984), and cases following it, federal courts are required to give deference to agency regulations and interpretations promulgated with respect to a statute that the agency has been entrusted by Congress to administer if they are not plainly erroneous or inconsistent with the statute or the regulations.[1] The Supreme Court has not addressed whether state courts owe the same degree of deference to federal agency regulations and interpretations. This case also presents the questions whether the Alabama Supreme Court's failure to defer and its misinterpretation of the HUD regulations requires reversal as an error of federal law and, under the circumstances, violates United's right to due process under law.

Petitioner, United, made a conventional, first-lien mortgage loan of $31,827.76 to Mr. and Mrs. McGehee in June 1991.[2] A real-estate secured loan that is not insured under the National Housing Act or any other federal program is com-

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[1] Of course, such deference is due only to the extent a regulation or an interpretative ruling is not legislative and, therefore, does not violate the Administrative Procedure Act's notice and comment requirements that apply to substantive rule changes. *See* Administrative Procedure Act § 4, 5 U.S.C. § 553 (1994); *Chrysler Corp. v. Brown*, 44 U.S. 281, 303 (1979); *American Hosp. Ass'n v. Bowen*, 834 F.2d 1037, 1045-46 (D.C. Cir. 1987).

[2] The loan was made to consolidate certain outstanding credit obligations and an existing first and subordinate mortgage loan with annual interest rates ranging from 10% to over 19%.

monly called a conventional loan. The loan originated out of United's Mobile, Alabama branch office but was underwritten, approved and funded through United's corporate office in Louisiana. The McGehees agreed to pay United certain "non-refundable mortgage origination fees" in consideration for making the loan. The McGehees paid origination fees in the amount of $2,779.24 or approximately 8% of the original loan amount. Such loan origination fees, often paid at time of closing in lieu of a higher interest rate, are commonly known as points.

The McGehees brought suit against United in the Mobile Circuit Court claiming that United violated § 5-19-4(g) of the Alabama Consumer Credit Code (commonly referred to as the Mini-Code) which limits the amount of points a lending institution may charge to 5% of the loan amount. Ala. Code § 5-19-4(g) (1994). However, the Mini-Code also exempts a lending institution from the licensing obligation (imposed elsewhere in the Mini-Code) and most of the practice restrictions, including the points limitation of § 5-19-4(g), if it "is an approved mortgagee under the provisions of the National Housing Act." Ala. Code § 5-19-31(a) (1994). Failure of the creditor to comply with any requirements of the Mini-Code could result in the forfeiture of interest paid on the loan. Ala. Code § 5-19-19(c); and *Farmer v. Hypo Holdings, Inc.*, 1995 WL 664589 (Ala. Nov. 9, 1995) (opinion withdrawn and superseded on rehearing).

The National Housing Act is a federal statute. See 48 Stat. 1246 (codified as periodically amended at 12 U.S.C. § 1701-1750g (1994)). Congress delegated to HUD the authority to promulgate regulations implementing the National Housing Act. 12 U.S.C. § 1715(b) and 42 U.S.C. § 3535(d). Accordingly, whether a lender is an approved mortgagee under the National Housing Act, and therefore exempt from Ala. Code § 5-19-4(g), is determined by HUD regulations. *See* 24 C.F.R. § 202.11(a).[3]

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[3] 24 C.F.R. Part 202 is the current location of the relevant HUD regulations relating to National Housing Act approved mortgagees. In 1990 when HUD approved United as a National Housing Act "approved

The Division of Lender Approval of HUD's Office of Lender Activities and Program Compliance, located in Washington, D.C., approved United as a "nonsupervised mortgagee" on October 3, 1990. As a "nonsupervised mortgagee," United was approved to originate 1-4 family residential mortgage loans and submit applications to HUD for mortgage insurance under the National Housing Act. *See* 24 C.F.R. § 202.14.

Since being approved, United has annually satisfied all requirements in order to remain in good standing as an approved mortgagee. Accordingly, HUD has verified to United that United remains an "approved mortgagee" under the provisions of the National Housing Act. App., G-3 to G-4.

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mortgagee," the regulations setting forth the requirements for approval were located at 24 C.F.R. § 203, in particular § 203.4. There are some differences between the regulations as they existed in 1990 , the 1994 regulations on which the Alabama Supreme Court based its decision, and the current regulations in 24 C.F.R. Part 202. Unless there is a material difference, United will simply cite to the 1994 regulations.

24 C.F.R. § 202.11(a)(1) provides that:

[a] mortgagee may be approved for participation in the mortgage insurance programs authorized by the National Housing Act ... upon filing a request for approval on a form prescribed by the Secretary [of HUD] and signed by the applicant.... Approval of the application by the Secretary shall constitute:

(i) The Secretary's agreement that the mortgagee shall be considered an approved mortgagee except as otherwise ordered by the Mortgagee Review Board, or an officer or subdivision of the Department of Housing and Urban Development to which the Mortgage Review Board has delegated its power, unless the mortgagee voluntarily relinquishes its approval;

(ii) The mortgagee's agreement to comply at all times with the General approval requirements of § 202.12, and the special requirements for the class of mortgagee, at §§ 202.13, 202.14, 202.15, 202.16 or 202.17, for which it was approved; and,

(iii) An origination approval agreement under which approval to originate mortgages for insurance may be terminated as provided in paragraph (d) of this section.

24 C.F.R. § 202.11(a)(1) (1994).

On cross-motions for summary judgment, United moved for judgment on the issue of whether it was an "approved mortgagee" under the National Housing Act and therefore exempt from the licensing and certain practice requirements of the Mini-Code, including the § 5-19-4(g) points limitation. The Circuit Court found that United was an "approved mortgagee" pursuant to HUD regulations implementing the National Housing Act. App., A-3, A-6. Nonetheless, it held that United was not exempt from the points limitation contained in § 5-19-4(g) because the McGehee's loan was not a federally insured loan. According to the Mobile Circuit Court, the exemption applies only to federally insured loans not to conventional loans, even if they are made by HUD approved mortgagees. App., A-6 to A-8. United appealed.

In its original opinion of March 22, 1996, the Supreme Court of Alabama acknowledged that it was undisputed that United was an "approved mortgagee" under the National Housing Act when it made the loan to the McGehees. The Alabama Supreme Court held that, under the plain meaning of § 5-19-31(a), United was exempt from the points limitation regardless of whether the loan was conventional or insured under the National Housing Act. App., B-6 to B-8.

The McGehees then petitioned for rehearing. The McGehees argued on rehearing that United's Mobile branch office was not independently approved pursuant to 24 C.F.R. § 202.12(m)[4] to submit applications for mortgage insurance,

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[4] HUD issued an interim rule on January 26, 1996, proposing to amend 24 C.F.R. § 202.12(m). 61 Fed. Reg. 2650 (1996). The interim rule took effect on February 26, 1996, before the Alabama Supreme Court issued its original opinion in March of 1996. *Id.* The amendment to § 202.12(m) was made final on August 9, 1996, after the Supreme Court's original opinion but before its opinion on rehearing. 61 Fed. Reg. 36452 (1996). Section 202.12(m), as amended, provides that National Housing Act "approved mortgagees" need not obtain separate approval for their branch offices in order to issue National Housing Act insured loans out of those offices. All that is required is for the lender to register its branch offices with the Secretary. The Alabama Supreme Court's rulings were all premised on earlier versions of § 202.12(m) which permitted an approved mortgagee to obtain approval of branch offices to submit applications for mortgage insurance. 12 U.S.C. § 202.12(m) (1994). Separate approval

and that the exemption in § 5-19-31(a) did not apply to United in this case. The McGehee had not raised this issue previously. Nevertheless, the McGehees argument sought to interpret the reach of the exemption in the state statute and not the meaning of the federal regulations. The McGehees never claimed that United's Mobile branch office was entirely free of HUD regulations simply because it was not independently approved to offer National Housing Act insured loans. Nor did they argue that United, as an institution, was not a HUD approved mortgagee as defined by HUD regulations.

In response, United argued that because HUD had approved it, as an institution, to participate as a mortgagee under the National Housing Act, its status as approved mortgagee satisfied the plain meaning of § 5-19-31(a). Section 5-19-31(a) simply states that an exemption is provided when the "creditor is a lending institution which is an approved mortgagee under the provisions of the National Housing Act." Ala. Code § 5-19-31(a)(1994). Consequently, United argued that it was exempt from § 5-19-4(g), regardless of whether or not the Mobile branch office was independently approved.

The Alabama Supreme Court, on October 11, 1996 withdrew its original opinion and filed a new opinion holding that United was not an "approved mortgagee" under the National Housing Act. The court therefore held that United was not exempt from the § 5-19-4(g) points limitation and that the Circuit Court properly granted summary judgment in favor of the McGehees on this issue. App., C-17. The Alabama Supreme Court's opinion is based on an extensive review and interpretation of HUD's regulations. App., C-7 to C-17. The court erroneously concluded that because United's Alabama offices were not approved by HUD they were not regulated by HUD. App., C-10, C-14 The court concluded that HUD regulation and supervision over United as an approved mortgagee did not extend to a branch office that was not inde-

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for branch offices to submit applications for National Housing Act insurance did not affect a lending institution's status as an approved mortgagee; or affect the mortgagee's ability to make conventional mortgage loans.

pendently approved pursuant to 24 C.F.R. § 202.12(m). App., C-14 to C-17.

The Alabama Supreme Court's foray into federal law was unforeseen and unwarranted. The McGehees sought to narrow the applicability of § 5-19-31(a) by arguing for additional limitations not contained in the statutory language. These arguments were not based on an interpretation of the federal regulations. The Alabama Supreme Court, however, based its decision squarely on an interpretation of federal regulations relating to whether HUD's regulations and oversight apply to United's Mobile office. App., C-7 to C-17.

United petitioned for rehearing and presented the Alabama Supreme Court with HUD's interpretation of its own regulations. United argued that the Alabama Supreme Court was required to defer to HUD's interpretation of its own regulations, under the principles announced by this Court in *Chevron*. United also argued that the Alabama Supreme Court's opinion on rehearing was both erroneous as a matter of federal law and resulted in a due process violation. United's Petition for Rehearing at 1-2, 28-33. This was United's first opportunity to address these questions because they had never previously been at issue. HUD has stated that t a HUD/National Housing Act approved mortgagee is subject to HUD regulation and control with respect to its lending activities irrespective of whether it makes National Housing Act insured loans or conventional loans or whether a branch office has been independently approved by a HUD Field Office pursuant to 24 C.F.R. § 202.12(m). App., G-1 to G-2. An opinion letter from an administrative agency's counsel may be treated as an official administrative interpretation. *See Thorpe v. Housing Authority of Durham*, 393 U.S. 268, 276 (1969); *Udall v. Tallman*, 380 U.S. 1, 16 (1965); *Brubaker v. Morton*, 500 F.2d 200, 202 (9th Cir. 1974).

In its petition for rehearing, United urged the court to consider and defer to HUD's interpretation that United is an approved mortgagee and that HUD's regulations apply to "approved mortgagees" under the National Housing Act regardless of whether the mortgagee has elected to obtain HUD

approval for any one of its branch offices under 24 C.F.R. § 202.12(m). United further informed the Alabama Supreme Court that failing to defer to HUD regulations and interpretations implicated serious issues of federal supremacy. Despite this invitation to consider HUD's regulations and interpretations and United's assertion of the federal questions raised here, the Alabama Supreme Court denied United's petition for rehearing.[5] App., D-1.

REASONS FOR GRANTING THE PETITION

Federal courts are required to defer to federal agency regulations as correctly stating the law unless those regulations are arbitrary, capricious, or manifestly contrary to statute. They must likewise defer to a federal agency's interpretation of those regulations as correctly stating the law unless plainly erroneous or inconsistent with the regulation, or

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[5] This case does not fall within the principle, reaffirmed recently in *Adams v. Robertson*, 65 U.S.L.W. 4180, 4181 n. 3 (Mar. 3, 1997), that ordinarily it is too late to present a federal question to a state court for the first time in a rehearing petition. *Adams* and the cases upon which it relies are distinguishable because the federal question in those cases could have been raised at an earlier stage of the proceedings. Here, the federal question did not become relevant until the Alabama Supreme Court, for the first time in granting the McGehee's rehearing petition, invoked on its own an erroneous interpretation of the HUD regulations which had not been argued by the McGehees. The Alabama Supreme Court thus unforseeably raised the federal questions presented here. This case, therefore, is within the exception recognized in *Saunders v. Shaw*, 244 U.S. 317 (1916), a case involving an identical procedural context in that the federal issue did not arise until the state supreme court filed an opinion on rehearing so that the first opportunity to raise the question was on a second rehearing application which the state court denied without opinion. There, this Court stated, "when the act complained of is the act of the supreme court, done unexpectedly at the end of the proceeding ... it would leave a serious gap in the remedy for infraction of constitutional rights if the party aggrieved in such a way could not come here." *Id.* at 320. Therefore, the Court held that the petitioner should not be required to anticipate such an unexpected decision and that the federal question was presented timely and would be considered even though not expressly addressed by the state court in denying the second rehearing petition. *See also American Surety Co. v. Baldwin*, 287 U.S. 156, 164 (1932).

issued in a manner inconsistent with the rulemaking provisions of the Administrative Procedures Act.

Properly promulgated federal regulations are laws of the United States and as such are within the Supremacy Clause of the Constitution. Therefore, a federal agency's regulations are within the supreme law of the land to the extent they are neither arbitrary, capricious or manifestly contrary to statute. Agency interpretations are likewise within the supreme law of the land unless plainly erroneous or inconsistent with the regulation. State courts must be required to defer to those regulations and interpretations when deciding a question of federal law.

This Court should grant certiorari to declare that the Supremacy Clause of the United States Constitution requires state courts to defer to federal agency regulations and interpretations on matters of federal law to the same extent as required of federal courts. As such, federal agency regulations and interpretations will be binding on state courts deciding questions of federal law. Because of the growth of administrative agencies as an agent of Federal government, it is imperative that federal agency regulations and interpretations receive consistent and uniform treatment.

In the absence of such a declaration, national uniformity within regulatory schemes, one of the driving motives for delegation of responsibility to an administrative agency, will be threatened by divergent state court interpretations. This will lead to confusion, the possibility of inconsistent obligations in different states and create opportunities for pernicious forum shopping.

Furthermore, this Court should grant certiorari to correct the Alabama Supreme Court's incorrect interpretation of the HUD regulations. This misinterpretation violated United's right to due process.

I. Federal Courts Must Defer to Federal Agency Regulations and Agency Interpretations

This Court has made clear that when Congress explicitly delegates responsibility to an agency to implement a statute by regulation, the federal courts are to give these legislative

regulations, when properly issued, "controlling weight unless they are arbitrary, capricious, or manifestly contrary to the statute." *Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 843-44 (1984). "The power of an administrative agency to administer a congressionally created ... program necessarily requires the formulation of policy and the making of rules to fill any gap left, implicitly or explicitly, by Congress." *Id.* at 843 (quoting *Morton v. Ruiz*, 415 U.S. 199, 231 (1974).

In nearly all of this Court's opinions stating this rule, the issue has been whether a lower federal court gave the required deference to the federal agency's regulations. *See e.g., Good Samaritan Hospital v. Shalala*, 508 U.S. 402 (1993); *Chevron*, 467 U.S. 837. No Supreme Court opinion has explicitly addressed the proper level of deference to federal agency regulations that is owed by state courts pursuant to the Supremacy Clause.

Nor has any Supreme Court case explicitly addressed the level of deference a state court owes to federal agency interpretations of those regulations. A federal agency's interpretation of its own regulations is entitled to substantial deference by the federal courts. *Thomas Jefferson Univ. v. Shalala*, 512 U.S. 504, ***, 114 S. Ct. 2381, 2386 (1994). The task for a federal court reviewing such an agency's interpretation of its regulations "is not to decide which among several competing interpretations best serves the regulatory purpose. Rather, the agency's interpretation must be given controlling weight unless it is plainly erroneous or inconsistent with the regulation." *Id.* (internal quotations omitted).

II. Federal Agency Regulations and Interpretations are Federal Law for Purposes of the Supremacy Clause

The "laws of the United States" that are protected by the Supremacy Clause "encompasses both federal statutes and statutorily authorized agency regulations." *Lynnbrook Farms v. Smithkline Beecham Corp.*, 79 F.3d 620, 623 (7th Cir.) (citing *City of New York v. F.C.C.*, 486 U.S. 57, 63 (1988)), *cert. denied*, 117 S.Ct. 178 (1996). Properly promulgated, substantive federal agency regulations are law and thus protected by the su-

premacy clause. *City of New York*, 486 U.S. at 63; *Chrysler Corp. v. Brown*, 441 U.S. 281, 295 (1979). "This doctrine is so well established that agency regulations implementing federal statutes may even pre-empt or supersede state law." *City of New York*, 486 U.S. at 63-64; *Chrysler Corp.*, 441 U.S. at 295-96.

Properly issued agency interpretations should likewise be entitled to protection under the Supremacy Clause as "laws of the United States." The regulatory implementation of a statutory scheme need not anticipate every eventuality and "all specific applications of a rule [need not] evolve by further, more specific rules rather than by adjudication." *Shalala v. Guernsey Memorial Hosp.*, 115 S. Ct. 1232, 1237 (1995). It is proper for an agency to issue guidelines or interpretative rules to elucidate its statutory mandate. *Id.*

Because the ultimate validity of both regulations and their interpretation is based on whether they comply with the statutory mandate to the agency, and the standards for determining this are functionally identical, an agency's interpretation of its own regulations should be federal law to the same extent as a regulation. The construction and application of a statute by the agency charged with its administration is entitled to substantial deference. *See Blum v. Bacon*, 457 U.S. 132, 141 (1982); *Brannan v. United Student Aid Funds, Inc.*, 94 F.3d 1260, 1263 (9th Cir. 1996) (held that Secretary of Education's interpretation of certain regulations was entitled to deference unless arbitrary, capricious or manifestly contrary to statute and therefore it pre-empted inconsistent state law), *petition for cert. filed*, 65 U.S.L.W. 3539 (Jan.29, 1997).

Regulations properly promulgated by federal agencies, and an agency's interpretations of such regulations are federal law within the Supremacy Clause, at least to the extent they are not arbitrary, capricious, manifestly contrary to statute, or plainly erroneous or inconsistent with the regulation. Accordingly, the Supremacy Clause must require that state courts defer to such regulations and interpretations to the extent they are federal law (i.e. to the extent they not arbitrary, capricious, manifestly contrary to statute, or plainly erroneous or inconsistent with the regulation).

Several state courts have recognized as much in conceding that the appropriate level of deference owed by state courts to federal agency regulations and interpretations is a matter of federal law and not state law. *Totemoff v. State of Alaska*, 905 P.2d 954, 967 (Alaska 1995) ("we apply federal law on deference in determining whether deference is owed to a federal agency's legal position"), *cert. denied*, 116 S.Ct. 2499 (1996); *Delorme v. North Dakota Dep't of Human Services*, 492 N.W.2d 585, 587 n.2 (N.D. 1992) ("Because we are dealing with interpretation of a federal statute and the deference due a federal agency's construction of that statute, we will apply the rules of construction set out by the federal judiciary."); *Matarazzo v. Rowe, Comm'r of Income Maintenance*, 623 A.2d 470, 481 (Conn. 1990); *Samara Dev. Corp. v. Marlow*, 556 So.2d 1097, 1102 (Fl. 1990) ("The law is clear that the interpretation of a federal statute by a federal agency authorized to do so must be given great deference.") (Overton, J. dissenting); *Ideal Federal Sav. Bank v. Murphy*, 663 A.2d 1272, 1280 (Md. 1995)

III. A State Court's Erroneous Interpretation of Federal Regulations is an Issue of Federal Law

This Court has held that when a state court's construction of a state statute is based on state law, its construction is conclusive, but that when a state court's construction of a state statute is based on federal regulations, it becomes a question of federal law. *Three Affiliated Tribes of the Fort Berthold Reservation v. Wold Engineering, P.C.*, 467 U.S. 138, 151-52 (1984); *Standard Oil Co. of California v. Johnson*, 316 U.S. 481, 483 (1942).

Standard Oil Co. of California v. Johnson involved the California Motor Vehicle Fuel License Tax Act[6] in which California imposed a tax on the distribution of motor vehicle fuel. 316 U.S. 482-83. Section 10 of that act exempted from the tax any "fuel sold to the government of the United States or any department thereof for official use." A distributor who

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[6] Cal. Stats. 1923, pp. 572-74; 1927, p. 1309; 1933, pp. 1636-37; St. 1935, p. 1696; 1937, p. 2219, Gen. Laws 1937, Act 2964.

sold fuel to United States Army Post Exchanges in California was nevertheless taxed on those sales. *Id.* at 482. The distributor paid under protest, and the Supreme Court of California held that U.S. Army Post Exchanges where neither a branch of the United States nor a department thereof. *Id.* at 482. On appeal, this Court noted that the relationship between these Post Exchanges and the United States was governed by regulations promulgated by the Secretary of War and was therefore a question of federal law, not state law. *Id.* at 483. Accordingly, the Court was not bound by the California Supreme Court's determination and reversed. *Id.*

Thus, although state court interpretations of state statutes are generally immune from Supreme Court review, it is "well established ... that this Court retains a role when a state court's interpretation of state law has been influenced by an accompanying interpretation of federal law." *Three Affiliated Tribes of the Fort Berthold Reservation*, 467 U.S. at 151-52. Where the state court has proceeded based on an incorrect perception of federal law, it is this Court's practice to vacate the judgment of the state court and remand the case to allow the court to reconsider the issue free from its mistaken understanding of the federal law. *Id.*

Furthermore, pursuant to established practice, where "a state court decision fairly appears ... to be interwoven with the federal law, and when the adequacy and independence of any possible state law ground is not clear from the face of the opinion, [the Court] will accept as the most reasonable explanation that the state court decided the case the way it did because it believed the federal law required it to do so." *Michigan v. Long*, 463 U.S. 1032 (1983); *see also Pennsylvania v. Labron*, 116 S. Ct. 2485, 2487 (1996).

Thus, in this case, the Alabama Supreme Court's decision, which is interwoven with, if not completely based on, federal law must be reversed to the extent it misinterpreted federal law.

IV. The Alabama Supreme Court's Failure to Defer to HUD Regulations and Interpretations Caused it to Misinterpret Federal Regulations and to Violate United's Due Process Rights

The Alabama Supreme Court's decision is premised on its holding that "[b]ecause United's Mobile office is not an approved branch office, ... [HUD] requirements do not apply to any offices it has in Alabama."[7] App., C-10. Stated more simply, the court believed that "because United's Alabama offices are not approved by HUD, they are not regulated by HUD." App., C-14.

A. The Alabama Supreme Court's Failure to Defer to HUD Regulations and Interpretations Led it to Err

As a result of this mistaken understanding the Alabama Supreme Court held that "United is not a lending institution which is an approved mortgagee under the provisions of the National Housing Act ... because, as to its operations in Alabama to which [Ala. Code §§ 5-19-4(g) & 5-19-31(a)] might apply, United is not such an 'approved mortgagee.'" App., C-17. Based on this assumption, the Alabama Supreme Court incorrectly ruled that United is not an approved mortgagee under the National Housing Act. App., C-17.

The Alabama Supreme Court's interpretation is inconsistent with HUD's. HUD's interpretation was timely presented to the Alabama Supreme Court. HUD has stated that the "requirements of 24 C.F.R. §§ 202.12 and 202.14 apply to an approved mortgagee under the provisions of the National Housing Act when it originates non-FHA insured (i.e. "conventional") loans[]"and that these "same requirements ... ap-

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[7] The specific requirements the Alabama Supreme Court had in mind were the "yearly verification reports; experience and qualifications of employees, including branch office managers; staffing and facilities requirements; communications capability and responsibility; restrictions on escrow accounts; responsibility for originating and servicing mortgages in accordance with HUD requirements; and net worth requirements." App., C-10.

ply if the same mortgagee originates the same conventional loans, but in a geographic area that has not been designated under 24 C.F.R. § 202.11(a)(4) or approved under 24 C.F.R. § 202.12(m)[.]" App., G-1 to G-2.

It makes eminent sense for HUD to interpret its regulations to require HUD/National Housing Act approved mortgagees to comply with HUD regulations regardless of whether they actually issue National Housing Act insured mortgage loans or merely conventional ones and regardless of whether those loans are originated from an approved area or not. Being HUD approved conveys to the public that the mortgagee is competent, reliable and trustworthy. Furthermore, it accomplishes the purpose of casting HUD's regulatory control wider than otherwise and thus enables HUD to promote its goals of extending housing, at fair, equitable and competitive rates to a greater proportion of the population than at present. Last, this interpretation is not inconsistent with or otherwise precluded by the National Housing Act or any of the regulations promulgated by HUD.

HUD's interpretation of its regulations (ie. that United is an approved mortgagee and remains under HUD regulation and control regardless of whether it independently approves its branch offices or originates conventional loans) must, therefore, be treated as federal law because it is not arbitrary, capricious, manifestly contrary to statute, or plainly erroneous or inconsistent with the regulation. As federal law, the Supremacy Clause applies and prohibits the Alabama Supreme Court from interpreting the regulations in any other way. Therefore, the Alabama Supreme Court's interpretation is incorrect, violates the Supremacy Clause and the judgment resting on that interpretation must be vacated.

As the dissent from the October 11, 1996 opinion noted, "[i]n order to resolve the issue raised by the McGehees -- whether HUD approval to make federally insured loans in Alabama is a prerequisite to obtaining § 5-19-31(a) exemption -- [the Alabama Supreme Court] should have looked to federal law [i.e., HUD regulations and interpretations], which clearly establishes that United is a HUD-approved mortgagee

regardless of whether it seeks 'branch approval' for any of its local offices." App., C-18 to C-19. This refusal to consider, let alone defer to HUD regulations and interpretations led the court into an incorrect construction of the HUD regulations in violation of the Supremacy Clause.

This misinterpretation of the HUD regulations led to an adverse judgment against United and violated United's right to due process under law.

B. The Alabama Supreme Court Violated United's Rights to Due Process Under Law

The bedrock principle of due process of law, as required by the Fourteenth Amendment is that parties must have "fair notice" of what conduct is forbidden by the state. *BMW of North America, Inc. v. Gore*, 116 S. Ct. 1589, 1598 (1996); *United States v. Harris*, 347 U.S. 612, 617 (1954). Thus, the due process clause may be implicated by a statute that is vague or overbroad and does not give adequate notice of what particular conduct is prohibited. *See Bouie v. City of Columbia*, 378 U.S. 347, 352 (1963). Likewise, in *Gore*, the defendant, BMW, had notice that it might be subject to punitive damages, but this Court still found a deprivation of due process, because BMW did not have adequate notice of the amount of any punitive damages award and there were no adequate controls imposed on jury discretion to ensure that punitive damages be kept within foreseeable limits.

As this Court has recognized, the deprivation of due process is even greater when a statute that is not vague or imprecise, but is in fact clear and unambiguous, leading parties to rely on it, is interpreted in an unforeseeable manner and applied retroactively to those parties to condemn conduct reasonably believed to be permitted. *Bouie*, 378 U.S. at 352-53. "There can be no doubt that a deprivation of the right of fair warning can result not only from vague statutory language but also from an unforseeable and retroactive judicial expansion of narrow and precise statutory language." *Id.* at 352.

United had no advance notice and could have had no notice that the Alabama Supreme Court would interpret the exemption provision of Ala. Code § 5-19-31(a) in a manner not

disclosed by the plain meaning of that statute and apply such interpretation retroactively. This interpretation made conduct previously exempt from regulation a violation of the Ala. Code § 5-19-4(g) points limitation, subjecting United to severe and onerous penalties that could result in the forfeiture of interest paid on the McGehee's loan and other loans originated in Alabama since becoming a HUD approved mortgagee. In addition, United could not have known that the court would base its decision on an incorrect interpretation of federal law.

The McGehees did not request a finding that HUD regulations and oversight do not apply to loans made out of branch offices that are not independently approved pursuant to 24 C.F.R. 202.12(m). The court, on its own initiative and without notice, decided this case by interpreting HUD regulations rather than the state statute. Furthermore, the court's interpretation of the HUD regulations is incorrect. Thus United was doubly blind to the result. It could not foresee that the court would decide on federal grounds rather than state law. Further, even if it could have foreseen the federal issue, it could not have foreseen the court's interpretation of federal regulations which is in direct contradiction to HUD's interpretation of those regulations.

The Alabama Supreme Court's limitation of the exemption of Ala. Code § 5-19-31(a) to approved mortgagees who have an approved branch in Alabama was unforeseeable. The plain terms of the statute exempt "approved mortgagees" and HUD has stated that United is an "approved mortgagee." App., G-3 to G-4. Furthermore, the Alabama legislature reenacted the exemption found in § 5-19-31(a) in 1979, 1989, 1994 and 1996 without changing the nature of that exemption as it existed in 1973 when the Alabama Attorney General issued an opinion stating that "approved mortgagees" under the National Housing Act who make conventional loans are also exempt from state licensing. *See* Acts 1979, No. 79-328; Acts 1989, No. 89-541; Acts 1994, No. 94-118; and Acts 1996, No. 96-576. It is presumed that the legislature knew of the Attorney General's opinion and intended to give it the same con-

struction. *Farmer v. Hypo Holdings, Inc.*, 675 So.2d 387, 390 (Ala. 1996).

United had every reason to believe that its conduct was exempted from the points limitation of Ala. Code § 5-19-4(g). The Alabama Supreme Court's unprecedented and incorrect construction of HUD regulations led it to an erroneous determination that United was not in fact an "approved mortgagee" under the National Housing Act to the extent it did business in Alabama. This decision is not only incorrect but was unforeseeable. By applying this decision retroactively to United, the Alabama Supreme Court failed to give adequate prior notice of what conduct is permitted and what conduct is prohibited by Ala. Code § 5-19-4(g).

V. The Questions Presented Are Important

Neither this Court, nor any of the United States Courts of Appeals have addressed the standard that a state court must apply when determining whether to defer to a federal agency's regulations and interpretations. As more responsibility is delegated to federal administrative agencies, the need to ensure the uniformity of law created and enforced by those agencies grows. Likewise, to the extent that federal regulations conflict with or otherwise interact with state law, the state courts need clear guidance on how to determine when and the extent to which they are bound by the Supremacy Clause to give effect to properly issued federal agency regulations and interpretations.

Furthermore, because appeals from state courts may not be heard in the lower federal courts, this Court is the only federal forum in which such a rule may be pronounced and enforced. Thus, this is not a question that can be decided by the Federal District Courts or the Courts of Appeal for the various circuits. Under this Court's Rooker/Feldman abstention doctrine, a party losing in state court is barred from seeking what in substance would be appellate review of the state judgment in a United States District Court, based on the losing party's claim that the state judgment itself violates the loser's federal rights. *See District of Columbia Court of Appeals v. Feldman*, 460 U.S. 462, 482 (1983); *Rooker v. Fidel-*

ity Trust Co., 263 U.S. 413, 416 (1923). A necessary corollary to the Rooker/Feldman doctrine is that this Court is the only proper federal forum within which to seek review of a state court's incorrect opinions. Accordingly, only this Court has a chance to review and determine the degree of deference state courts must give to federal agency regulations and interpretations. This case presents a rare opportunity in which to enunciate a rule governing such determinations.

If this Court denies certiorari, state courts will remain without guidance on the degree of deference they are required to give federal agency regulations and interpretations. Without any clear guidance, various state courts may fail to give adequate deference and, as a result, may incorrectly decide that a federal agency's regulations or interpretations are not correct and are not binding on it in deciding a question of federal law. Inconsistent judgments and requirements may prevent federal agencies from uniformly applying their regulations and may confuse persons as to the correct rule of law. Furthermore, this may lead to forum shopping by litigants in an attempt to avoid federal agency regulations, and conflicting standards for those subjected to federal regulation.

To the extent plaintiffs engage in forum shopping and do not plead issues of federal law in their complaints, the well pleaded complaint rule will prevent defendants from removing these issues to the federal courts. Thus, the federal courts may be frustrated in their attempts to decide important issues of federal law and to correct erroneous interpretations in the state courts.

In addition, the Alabama Supreme Court's decision is based on an incorrect interpretation of federal regulations. This decision and the resulting interpretation of Ala. Code §§ 5-19-4(g) and 5-19-31(a) was completely without any advance notice or warning. The adverse judgment against United and the application of § 5-19-4(g) to United therefore violated its due process rights.

Finally, review of this case is of particular importance to the secondary mortgage markets and other mortgage lenders. Home mortgage loans are actively traded in a secondary

mortgage market of national scope and size.[8] By introducing market forces and efficiencies this secondary market lowers the rate at which mortgage loans are initially offered to home buyers.[9] This secondary market places great reliance on national uniformity of documents and the meaning of the language in them so that investors can have confidence in the integrity of their investments.[10] Other HUD-approved mortgagees who relied on § 5-19-31(a) to make mortgage loans in Alabama could face the same deprivations as United. The Alabama Supreme Court's ruling threatens the uniform meaning of the term HUD/National Housing Act approved mortgagee and thus the stability and integrity of the secondary mortgage loan markets.

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[8] Franklin D. Cordell, Note, The Private Mortgage Insurer's Action for Rescission for Misrepresentation: Limiting a Potential Threat to Private Sector Participation in the Secondary Mortgage Market, 47 Wash. & Lee L. Rev. 587,587-94 (Summer 1990);Jo Anne Bradner, The Secondary Mortgage Market and State Regulation of Real Estate Financing, 36 Emory L.J. 971, 973-82 (Summer 1987); Robin Paul Malloy, The Secondary Mortgage Market A Catalyst for Change in Real Estate Transactions, 39 Sw. L.J. 991, 991-1001, 1013-18 (February, 1986).

[9] Cordell, supra note 6, at 593; Malloy, supra note 6, at 1013-16.

[10] Bradner, supra note 6 at 992-1003, 1007 (discussing need for uniformity of documents and for a uniform national law); Malloy, supra note 6 at 999, 1011-12, 1013-1020 (discussing need for national uniformity).

CONCLUSION

The petition for a writ of certiorari should be granted.

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March 6, 1997

IN THE
CIRCUIT COURT OF MOBILE COUNTY, ALABAMA

CV 93-1961

MICHAEL D. MCGEHEE, et al.,

Plaintiffs,

vs.

UNITED COMPANIES LENDING CORPORATION, et al.,

Defendants.

STATE OF ALA. MOBILE CO.
I certify that this pleading was filed
on May 11th 10:34 am 1995
/s/_____
Circuit Court

ORDER

This matter comes to the Court on Defendant United Companies Lending Corporation's ("UCLC") Motion for Summary Judgment and Plaintiffs' Motion for Summary Judgment as to Defendant UCLC's claim of exemption under Alabama Code § 5-19-31. Plaintiffs also submitted an objection and opposition to Defendant UCLC's Motion for Summary Judgment. This matter was heard March 30, 1995. After due consideration of the Motions and briefs submitted by counsel for both parties, pertinent case law and statutes cited therein, arguments of the parties, and Rule 56, Alabama Rules of Civil Procedure, the Court expressly finds that Defendant's Motion for Summary Judgment is due to be and is hereby DENIED. The Court further finds that Plaintiffs' Motion for Summary Judgment as to Defendant UCLC's claim of exemption under Alabama Code § 5-19-31 (a) is due to be and is hereby GRANTED.

DISCUSSION

Plaintiffs entered into a mortgage loan agreement with UCLC on June 21, 1991. The loan was secured by a first mortgage on plaintiffs' residence. The original principal balance of the loan was $34,800. The amount financed was $31,827.76. The following amounts appear on Plaintiffs' Truth-In-Lending disclosure statement:

(a) a "loan fee'' in the amount of $2779.24

(b) "Interim interest" in the amount of $133.50

(c) a "Tax Service Fee" in the amount of $59.50

These amounts together are denominated "Prepaid Finance Charges" and total $2972.24 which is approximately eight and one half percent (8.5%) of the original principal balance of the loan.[1]

Alabama Code § 5-19-1 through § 5-19-31 sets forth what is commonly referred to as the Mini-Code. The Mini-Code was enacted for regulatory purposes to protect the public, especially the consumer or debtor. *Derico v. Duncan*, 410 So.2d 27 (Ala. 1982). Section 5-19-4 (g) of the Mini-Code provides as follows;

> Notwithstanding the provisions of this or any other section of this chapter, a creditor may, pursuant to contract, in a consumer loan or consumer credit sale secured by an interest in real property, charge and collect points in an amount not to exceed five percent of the original principal balance in the case of a closed-end loan or credit sale, or five percent of the total line of credit in the case of an open-end credit

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[1] *See Exhibit A to Plaintiffs' Amended Complaint (Truth-In-Lending Disclosure Statement).* These amounts appear to fit squarely within the definition of "points" as set forth in Alabama Code § 5-19-4(g) and elaborated on in *Smith v. First Family Fin. Services*, 626 So.2d 1266 (Ala. 1993).

> plan. Points may be paid in cash at the time of the loan or credit sale, or may be deducted from the proceeds and included in the original principal balance. Points shall be in addition to all other charges and are fully earned on the date of the loan or credit sale and may be excluded from the finance charge for the purpose of computing the finance charge refund.

Plaintiffs allege that defendants violated section 5-19-4 (g) by assessing "points" in excess of five percent (5%) of the principal balance of the plaintiff's loan. Plaintiffs also contend that defendants falsely represented to plaintiffs that (i) UCLC was not subject to the Mini-Code when in fact it is, (ii) the transaction was not governed by the Mini-Code when in fact it was, and (iii) UCLC could legally charge points in excess of 5% of the loan amount when in fact it could not. Finally, plaintiffs contend that defendants suppressed and/or concealed that UCLC was in fact subject to the Mini-Code.

Defendants argue that the express language of Mini-Code section 5-19-31 (a) exempts UCLC from the point cap set forth in section 5-19-4 (g). Defendants further argue that because UCLC is exempt, UCLC cannot have violated the Mini-Code and each of plaintiffs' claims must fail.

Alabama Code § 5-19-31 (a) provides as follows:

> The provisions of this chapter, except the provisions of subdivision (1) of Section 5-19-1 and Section 5-19-3, shall not apply to any loan, forbearance, credit sale, lease, or other transaction involving an interest in real property or the sale, lease, or mortgage of an interest in real property, where the creditor is a lending institution which is an approved mortgagee under the provisions of the National Housing Act....

It is undisputed that this is a loan/mortgage involving an interest in real property and that UCLC is an approved mortgagee under the provisions of the National Housing Act.

Plaintiffs proffer two arguments in opposition to Defendants' Motion for Summary Judgment and in support of their own Motion for Summary Judgment as to the exemption defense asserted by Defendants. First, they argue that UCLC is not exempt because the prefatory language of Mini-Code section 5-19-4(g) **["Notwithstanding the provisions of this or any other section of this chapter..."]** clearly provides that the "points" cap applies *notwithstanding* the National Housing Act mortgagee exemption found in section 5-19-31 (a).

Defendants respond by arguing that the plain language of a statute should be interpreted so as to make related statutes consistent. According to defendants, acceptance of plaintiffs' contention that Mini Code section 5-19-4(g) somehow overrides the exemption language of section 5-19-31 (a) would render these Mini-Code provisions inconsistent. Defendants also point out that section 5-19-31 (a) has been amended twice and had there been confusion or mistake, the legislature would have corrected the same.

Based on the plain language of Alabama Code § 5-19-31 (a) and the legislative history of this code section, this Court agrees that plaintiffs' first argument is without merit.

Plaintiffs' second argument is that the exemption found in section 5-19-31 (a) does not apply because UCLC has never in fact originated an FHA, VA, or HUD-insured loan and because the loan made to plaintiffs was not an FHA, VA, or HUD-insured loan. It is undisputed that UCLC has never in fact originated an FHA, VA, or HUD-insured loan. It is also undisputed that this particular transaction between Plaintiff and Defendants was not an FHA, VA, or HUD-insured loan. Furthermore, it is undisputed that this particular transaction between plaintiffs and defendants is not insured by the Secretary of Housing and Urban Development or any other officer or agency of the federal government.

Defendants again respond by relying on the plain language of section 5-19-31. According to defendants, section 5-

19-31 limits the applicability of section 5-19-4 (g) by expressly exempting certain creditors from the five percent cap on discount points. Defendants point out that UCLC is "an approved mortgagee under the provisions of the National Housing Act" and that the loan transaction about which the plaintiffs complain involves the mortgage of an interest in real property. They also direct this Court's attention to the fact that the discount point provision is not contained in either section 5-19-1(l) or section 5-19-3 of the Mini-Code. Thus, they argue, it is absolutely clear that the transaction between the plaintiffs and UCLC is exempt from the discount point provision. They further argue that whether UCLC originates FHA, VA, or HUD-insured loans is irrelevant and does not affect UCLC's purported exemption.

UCLC cites *Casey v. Travelers Insurance Co.*, 531 So.2d 846 (Ala. 1988) for the proposition that the exemption language found in section 5-19-31 (a) should be given its plain meaning. Based on *Casey*, UCLC argues that section 5-19-3l (a) confers on "an approved mortgagee under the provisions of the National Housing Act" a blanket exemption from all provisions of the Mini Code except subdivision (1) of section 5-19-1 and section 5-19-3. Thus, UCLC argues that section 5-19-3l (a) is clearly analogous to section 5-19-22 [the Mini-Code section at issue in *Casey*] which was held to confer on life insurance companies a blanket exemption from the licensing provisions of the Mini-Code. In *Casey*, the Supreme Court recognized a blanket exemption for life insurance companies even though it was not clear whether the defendant life insurance company made consumer loans in its capacity as a life insurer or in some other capacity. Defendants assert that *Casey* dictates recognition of UCLC's purported exemption.

STANDARD OF REVIEW

Pursuant to Rule 56 of the Alabama Rules of Civil Procedure, a trial court may grant a summary judgment motion when (1) there is no genuine issue of material fact, and (2) the

moving party is entitled to a judgment as a matter of law. For purposes of the Motions before this Court, the Court expressly finds that there is no genuine issue of material fact. The dispositive issue before this Court is purely one of law and, as such, is proper for resolution by this Court. See *Studdard v. South Central Bell*, 356 So.2d 139 (Ala. 1978) and *O'Neal v. Macon Co. Board of Education*, 484 So.2d 401 (Ala. 1986). Specifically, a ruling on Defendant UCLC's Motion for Summary Judgment and a ruling on Plaintiffs' Motion for Summary Judgment as to the exemption defense necessarily depends on this Court's interpretation of the exemption language contained in Mini-Code section 5-19-31 (a). If the Court finds as a matter of law that UCLC is exempt from the points cap, then the Court must enter summary judgment in favor of defendant UCLC. If, on the other hand. the Court finds as a matter of law that UCLC is not exempt from the points cap, then the Court must enter summary judgment for plaintiffs on the issue of exemption.

CONCLUSIONS OF LAW

Mini-Code section 5-19-3l (a) expressly exempts any loan, mortgage or other transaction involving an interest in real property "where the creditor is a lending institution which is an approved mortgagee under the provisions of the National Housing Act." While it is undisputed that UCLC is an approved mortgagee under the provisions of the National Housing Act, it is also undisputed that *this particular transaction* between Plaintiffs and Defendants was *not* an FHA, VA, or HUD-insured loan. Furthermore, it is undisputed that *this particular transaction* between plaintiffs and defendants is *not* insured by the Secretary of Housing and Urban Development or any other officer or agency of the federal government.

Although defendants would have this Court hold that section § 5-19-31(a) provides a blanket exemption for any entity which is an approved mortgagee under the National

Housing Act, it is readily apparent from both the heading and the plain language of § 5-19-31 (a) that this section of the Mini-Code exempts particular transactions, not entities. Thus, the matter before this Court is distinguishable from *Casey*. In *Casey*, section 5-19-22 was the focus of the Court's holding that life insurance companies are exempt from licensing under the Mini-Code. Section 5-19-22 of the Mini-Code provides as follows:

> (a) No creditor shall engage in the business of making consumer loans or taking assignments of consumer credit contracts without first having obtained a license for each location from the administrator; provided, however, ... life insurance companies and federally constituted agencies shall be exempt from such licensing.

Section 5-19-22 clearly and unequivocally exempts life insurance companies from the licensing provisions of the Mini-Code whereas the Mini-Code section at issue in this case [5-19-31 (a)] clearly and unequivocally exempts particular transactions. Section 5-19-31 (a) clearly does not provide a blanket exemption for certain entities as does the licensing statute at issue in *Casey*. Accordingly, *Casey* is inapposite to the matter before this Court.

This Court is mindful of the goal of the Mini-Code toward consumer protection as stated in *Derico v. Duncan*, 410 So.2d 27 (Ala. 1982). It is also mindful of our Supreme Court's suggestion that the Mini-Code be construed with the protection of the consumer in mind. *See, e.g., Spears v. Colonial Bank of Alabama*, 514 So.2d 814 (Ala. 1987). To interpret the exemption language of section 5-19-3(a) as defendants suggest would be contrary to the plain language of that code section and would allow the exemption provided under that section to frustrate the operation and effectiveness of the Mini-Code. Moreover, defendants' interpretation of the exemption language, if accepted by this Court, would fla-

grantly violate the spirit of the Mini-Code and the legislative purpose for which it was enacted. *See, e.g., IMED Corp. v. Systems Engineering Associates Corp.*, 602 So.2d 344 (Ala. 1992) and *Derico v. Duncan*, 410 So.2d 27 (Ala. 1982).

Accordingly, this Court interprets Alabama Code § 5-19-3l(a) as exempting from all sections of the Mini-Code except the provisions of subdivision (1) of Section 5-19-1 and Section 5-19-3 only those loans, mortgages or other transactions involving an interest in real property actually made pursuant to, under, in connection with or subject to the provisions of the National Housing Act by a creditor that is an approved mortgagee under the provisions of said Act.

Based on this Court's interpretation of Alabama Code § 5-19-31 (a), the Court finds that Plaintiffs' Motion for Summary Judgment on the issue of the exemption defense is due to be and is hereby GRANTED and that Defendants' Motion for Summary Judgment is due to be and is hereby DENIED.

Pursuant to Rule 5 (a) of the Alabama Rules of Appellate Procedure, this Court expressly finds that this interlocutory order involves a controlling question of law as to which there is substantial ground for difference of opinion, that an immediate appeal from this order would materially advance the ultimate termination of the litigation and that the appeal would avoid protracted and expensive litigation. The Court also finds that a permissive appeal pursuant to Rule 5 (a) is warranted because the matter before this Court is one of first impression and final determination of the issues involved could have wide-ranging implications for all parties. The petition for permission to appeal shall be filed with the clerk of the Supreme Court within fourteen (14) days after the entry of this Written Order.

Defendant United Companies Lending Corporation has agreed to and is hereby **ORDERED** to reamortize plaintiffs' loan in compliance with Alabama Code § 5-19-4(g) and to collect only those amounts allowed thereunder during the

pendency of this appeal and until final ruling by the Alabama Supreme Court.

It is so **ORDERED** this 11th day of May, 1995.

/s/_____
Chris N. Galanos
Circuit Judge

STATE OF ALA.
MOBILE CO.
I certify that this pleading was filed on May 11th 10:34 a.m. 1995.
/s/_____
Circuit Court

NOTICE: This opinion is subject to formal revision before publication in the advance sheets of *Southern Reporter*. Readers are requested to notify the Reporter of Decisions, Alabama Appellate Courts, 300 Dexter Avenue, Montgomery, Alabama 36104-3741 ((334) 242-4621), of any typographical or other errors, in order that corrections may be made before the opinion is printed in *Southern Reporter*.

SUPREME COURT OF ALABAMA

OCTOBER TERM, 1995-1996

1941234

United Companies Lending Corporation

v.

Michael McGehee, et al.

Appeal from Mobile Circuit Court

(CV-93-1961)

Supreme Court of Alabama
Released Mar 22 1996
Clerk

HOUSTON, JUSTICE.

Pursuant to Rule 5, Ala.R.App.P., we permitted the defendant, United Companies Lending Corporation ("United"), to appeal from the interlocutory order of the Mobile County Circuit Court denying its motion for summary judgment and entering a partial summary judgment for the plaintiffs, Michael and Joyce McGehee. We reverse and remand.

The McGehees obtained a $34,800 loan from United for the purpose of consolidating certain pre-existing debts. United is an approved lender under the National Housing Act, 12 U.S.C. § 1701 et seq. The loan was secured by a mortgage on real estate. As part of their agreement with United, the McGehees agreed to pay a "loan origination fee" ("points") in an amount equal to eight percent of the original principal

amount of the loan. Following a series of disagreements with United concerning the proper amount and the timing of their payments, the McGehees filed this action, alleging fraud, among other things, and seeking damages and the rescission of the loan.

The McGehees base their claims on Ala. Code 1975, § 5-19-4(g), part of the Alabama Consumer Credit Act, Ala. Code 1975, § 5-19-1 et seq. ("Mini-Code"). Section 5-19-4(g), in pertinent part, provides:

> "Notwithstanding the provisions of this or any other section of this chapter, a creditor may, pursuant to contract, in a consumer loan ... secured by an interest in real property, charge and collect points in an amount not to exceed five percent of the original principal balance in the case of a closed-end loan."

They contended in the trial court, as they do here, that it is undisputed that United violated § 5-19-4(g) by charging and collecting from them points in an amount exceeding five percent of the original principal amount of the loan. Therefore, they argue, the trial court properly entered a partial summary judgment for them on this aspect of their claims. Relying on another provision in the Mini-Code, § 5-19-31(a), United contended in the trial court, and contends here, that its loan to the McGehees was not subject to the cap on points set out in § 5-19-4(g). Section 5-19-31(a), in pertinent part, provides:

> "The provisions of this chapter, except the provisions of subdivision (1) of Section 5-19-1 and Section 5-19-3 [which are not applicable in this case], shall not apply to any loan ... involving an interest in real property ... where the creditor is a lending institution which is an approved mortgagee under the provisions of the National Housing Act ...."

Thus, United argues that it was entitled to a judgment as a matter of law because, it says, it did not violate the Mini-Code

by overcharging on points and, it says, the allegation of such a violation formed the sole basis for the McGehees' claims.

The trial court's order was based on its conclusion that § 5-19-31(a) did not exempt United from complying with § 5-19-4(g), even though it is undisputed that United is an approved lender under the National Housing Act. The trial court's order reads, in pertinent part, as follows:

> "While it is undisputed that [United] is an approved mortgagee under the provisions of the National Housing Act, it is also undisputed that *this particular transaction* was not an FHA, VA, or HUD-insured loan....
>
> "Although [United] would have this Court hold that section 5-19-31(a) provides a blanket exemption for any entity which is an approved mortgagee under the National Housing Act, it is readily apparent from both the heading[1] and plain language of § 5-19-1(a) that this section of the Mini-Code exempts particular transactions, not entities....
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> "This Court is mindful of the goal of the Mini-Code [of] consumer protection as stated in *Derico v.*

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[1] Alabama Code 1975, § 1-1-14, provides:

"(a) The classification and organization of the titles, chapters, articles, divisions, subdivisions and sections of the Code, and the headings thereto, are made for the purpose of convenient reference and orderly arrangement, and no implication, inference or presumption of a legislative construction shall be drawn therefrom.

"(b) Unless otherwise provided in this Code, the descriptive headings or catchlines immediately preceding or within the text of the individual sections of this Code, except the section numbers included in the headings or catchlines immediately preceding the text of such sections, do not constitute part of the law, and shall in no manner limit or expand the construction of any such section. All historical citations and notes set out in this Code are given for the purpose of convenient reference, and do not constitute part of the law."

> *Duncan*, 410 So.2d 27 (Ala. 1982).... [United's] interpretation of the exemption language, if accepted by this Court, would flagrantly violate the spirit of the Mini-Code and the legislative purpose for which it was enacted....
>
> "Accordingly, this Court interprets Alabama Code § 5-19-31(a) as exempting ... only those loans, mortgages or other transactions involving an interest in real property actually made pursuant to, under, in connection with or subject to the provisions of the National Housing Act by a creditor that is an approved mortgagee under the provisions of said Act."

(Emphasis added by the trial court.) The dispositive issue on this appeal is, therefore, whether the trial court erred in ruling that United was not entitled to the exemption set out in § 5-19-31(a).

The fundamental rule of statutory review is to ascertain and give effect to the intent of the legislature in enacting a statute. Words used in a statute must ordinarily be given their natural, plain, ordinary, and commonly understood meaning, and where plain language is used a court is bound to interpret that language to mean exactly what it says. If the language of the statute is unambiguous, then there is no room for judicial construction and the clearly expressed intent of the legislature must be given effect. *IMED Corp. v. Systems Engineering Associates Corp.*, 602 So.2d 344 (Ala. 1992).

Sections 5-19-4 and 5-19-31 have their origins in the same act, which was approved on October 1, 1971. Ala. Acts 1971, No. 2052, p. 3290. Section 3 of Act No. 2052 was codified at § 5-19-4; § 25 of that act was codified at § 5-19-31. Act No. 2502 did not contain the provision relied on by the McGehees, which is now codified at § 5-19-4(g); the act did contain what is now codified at § 5-19-31(a), although the wording was slightly different:

> "None of the provisions of this Act, except provisions of Subsection (a) of Section 1 and Section 2 of this Act, shall apply to any loan ... involving an interest in real property ... where the creditor is a lending institution which is an approved mortgagee under the provisions of the National Housing Act."

On March 11, 1988, Act No. 88-87 was approved, with an effective date of June 30, 1988. Act No. 88-87 amended § 5-19-4 to provide for a five percent limitation on mortgage loan origination fees. That provision is codified at § 5-19-4(g).[2] *See Smith v. First Family Financial Services, Inc.*, 626 So.2d 1266 (Ala. 1993). Thereafter, § 5-19-31 was amended by Ala. Acts 1989, No. 89-541, p. 1132, § 1, which was approved on May 4, 1989, to include the addition of the following provision at subsection (d):

> "This Act is intended to confirm and clarify existing law that none of the provisions of this Chapter 19, other than the provisions of subdivision (1) of Section 5-19-1 and Section 5-19-3, apply to any transaction that is not a consumer transaction, or, where provided in Section 5-19-31(a) to any transaction involving an interest in real property whether or not a consumer transaction or to any transaction of a trust institution described in Section 5-19-31(a)."

Section 5-19-31 was again amended in 1994. See Ala. Acts 1994, No. 94-118, p. 146, § 1, which was approved on February 25, 1994. The 1994 amendment did make a substantive

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[2] Section 3 of Act No. 2052 was amended by Ala. Acts 1975, 4th Ex. Sess., No. 95, p. 2774, § 1; and § 5-19-4 was amended by Ala. Acts 1986, No. 86-304, p. 451, § 2; Ala. Acts 1988, 1st Ex. Sess., No. 88-942, p. 562, § 1; and Ala. Acts 1989, No. 89-525, p. 1074, § 1; however, none of those amendments is pertinent to our inquiry in this case.

addition to § 5-19-31; however, it made only nonsubstantive changes to the provision quoted above, which is now codified as follows at § 5-19-31(e):

> "This section is intended to confirm and clarify existing law that none of the provisions of this chapter, other than the provisions of subdivision (1) of Section 5-19-1 and Section 5-19-3, apply to any transaction that is not a consumer transaction, or, where provided in subsection (a) to any transaction involving an interest in real property, whether or not a consumer transaction, or to any transaction of a trust institution described in subsection (a)."

After carefully reviewing the record and the briefs, including the briefs filed by the amici curiae, we hold that United is entitled to the exemption set out in § 5-19-31(a). As the legislative history of §§ 5-19-4(g) and § 5-19-31(a) clearly shows, the legislature, after it had enacted the points cap on March 11, 1988, expressly reconfirmed and clarified on May 4, 1989, and again on February 25, 1994, that "none of the provisions of [Chapter 19], other than the provisions of subdivision (1) of Section l5-19-1 and Section 5-19-3 [not applicable here], apply ... to any transaction involving an interest in real property," as provided in § 5-19-31(a). Section 5-19-31(a) very clearly states that the provisions of Chapter 19, with certain exceptions not applicable here, "shall not apply to any loan ... involving an interest in real property ... where the creditor is a lending institution which is an approved mortgagee under the provisions of the National Housing Act." As previously noted, United is such an approved mortgagee.

Furthermore, according to the clear wording of § 5-19-31(a), "any loan" that involves an interest in real property where the creditor is an approved mortgagee under the provisions of the National Housing Act is exempt from the points cap set out in § 5-19-4(g). This Court has repeatedly reaffirmed the basic principle that words used in statutes ordinar-

ily must be given their natural, plain, ordinary, and commonly understood meaning. *IMED*, 602 So. 2d at 364. In determining the meaning of the statutory word "any," "'[this] court has several times interpreted ["any"] as importing ... wide signification—that it meant all, every, in the relation found.'" *Fuller v. Associates Commercial Corp.*, 389 So. 2d 506, 508 (Ala. 1980), quoting *Cole v. Sloss-Sheffield Steel & Iron Co.*, 186 Ala. 192, 65 So. 177 (1914) (rejecting the appellee's argument that the term "any mine" referred only to coal mines). In *Fuller* and in *Centennial Associates, Ltd. v. Clark*, 384 So. 2d 616 (Ala. 1980), both of which involved the interpretation of the word "any" as used in another Mini-Code provision, this Court rejected arguments for the adoption of a more narrow interpretation of the word "any," holding in *Fuller* that "[t]his Court must give effect to the legislature's choice of the word 'any' rather than judicially rewriting the statute." *Fuller*, 389 So. 2d at 509.

Section 5-19-31(a) is unambiguous. It exempts "any loan" involving an interest in real property where the creditor is "a lending institution which is an approved mortgagee under the provisions of the National Housing Act." The plain language "any loan" prohibits us from restricting this exemption to federally insured loans, as the trial court did. Courts are bound to interpret and apply statutes as they are written, and where plain language is used a court is bound to interpret that language to mean exactly what it says.[3]

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[3] On February 9, 1996, this Court, on application for rehearing in *Farmer v. Hypo Holdings, Inc.*, [Ms. 1940610, February 9, 1996] _____ So.2d _____ (Ala. 1996), reaffirmed the well-established rule of statutory construction "that an interpretation placed on a statute by an administrative agency charged with its enforcement will be given great weight and deference by a reviewing court." _____ So.2d at ____. The Alabama State Banking Department, which is responsible for administering this state's laws regulating or relating to the banking industry, filed an amicus curiae brief in this case in which it represented to this Court that it had always interpreted § 5-19-31(a) as we do today:

For the foregoing reasons, the trial court's order denying United's summary judgment for the McGehees is reversed, and the case is remanded for an order or proceedings consistent with this opinion.

REVERSED AND REMANDED.

Hooper, C.J., and Maddox, Almon, Shores, Kennedy, and Cook, JJ., concur.

> "One of the questions presented in this case is whether a mortgage loan made by a creditor which is an approved mortgagee under the provisions of the National Housing Act is subject to any provisions of the Mini-Code other than subdivision (1) of Section 15-19-1 and Section 5-19-3. ... The Banking Department, since the enactment of the Mini-Code, always has interpreted the Mini-Code to the effect that pursuant to the provisions of Section 5-19-31(a), mortgage loans made by a creditor which is an approved mortgagee under the National Housing Act are not subject to any provision of the Mini-Code other than subdivision (1) of Section 5-19-1 and Section 5-19-3. The Banking Department likewise always has interpreted the Mini-Code, including Section 15-19-31(a), not to require a Mini-Code license for a creditor which engages in the business of making mortgage loans where the creditor is an approved mortgagee under the National Housing Act."

Thereafter, based on our decision in *Farmer v. Hypo Holdings, Inc.*, even if we had found some ambiguity in § 5-19-31(a) or in the interaction of that section with § 5-19-4(g), our conclusion would nonetheless have been the same. Because the legislature is presumed to be aware of how an administrative agency has interpreted a statute, we consider the subsequent reenactment of a statute without material change to be a persuasive indicator that the legislature approves the agency's interpretation. _____ So.2d at _____. The legislature not only reenacted § 5-19-31(a) twice after it had enacted § 5-19-4(g), it specifically added a provision to "confirm" and "clarify" the law as interpreted by the State Banking Department.

NOTICE: This opinion is subject to formal revision before publication in the advance sheets of *Southern Reporter*. Readers are requested to notify the Reporter of Decisions, Alabama Appellate Courts, 300 Dexter Avenue, Montgomery, Alabama 36104-3741 ((334) 242-4621), of any typographical or other errors, in order that corrections may be made before the opinion is printed in *Southern Reporter*.

SUPREME COURT OF ALABAMA

OCTOBER TERM, 1996-1997

1941234

United Companies Lending Corporation

v.

Michael McGehee, et al.

Appeal from Mobile Circuit Court

(CV-93-1961)

On Application for Rehearing

Released
Oct 11 1996
Clerk
Supreme Court of Alabama

PER CURIAM.

The opinion of May 22, 1996, is withdrawn, and the following opinion is substituted.

Pursuant to Rule 5, Ala. R. App. P., this Court granted defendant United Companies Lending Corporation ("UCLC") permission to appeal from an interlocutory order denying its motion for a summary judgment and entering a partial summary judgment for the plaintiffs, Michael and Joyce McGehee. By entering the partial summary judgment, the circuit court disallowed UCLC'S defense by which it seeks to establish that § 5-19-31(a), Ala. Code 1975, exempts it from the

consumer protection provisions known as the Mini-Code, § 5-19-1 to -31, Ala. Code 1975--in particular, the 5% limit on discount points imposed by §5-19-4(g). The issue, as narrowed on rehearing, is whether a mortgagee that is not approved to make National Housing Act loans in Alabama comes within the provision of § 5-19-31(a) that "The provisions of this chapter ... shall not apply to any loan ... involving an interest in real property ... where the creditor is a lending institution which is an approved mortgagee under the provisions of the National Housing Act."[1]

In June 1991, UCLC made a loan to the McGehees and took a mortgage on their home as security. The McGehees borrowed $31,827.76; in determining the amount the McGehees were to repay, UCLC added to that amount $2,972.24 in prepaid finance charges. Of the prepaid finance charges, $2,779.24 was imposed as a "loan fee," which is a nonrefundable mortgage origination fee within the meaning of "points" as that term is used in § 5-19-4(g), see *Smith v. First Family Financial Services, Inc.*, 626 So. 2d 1266 (Ala. 1993). This amount of points is approximately 8% of the amount financed.[2]

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[1] The dissent asserts that this question was not presented to the circuit court. On the contrary, the McGehees' brief in opposition to UCLC's motion for summary judgment made the point that UCLC was not approved to make NHA loans in Alabama: "UCLC's 'approval' covers only the New Orleans HUD field office jurisdiction. On October 3, 1990, UCLC received its 'approval.'" That brief also states: "UCLC has not applied for branch approval for any of its branches to make HUD and/or National Housing Act loans. It is undisputed that UCLC has not obtained separate HUD approval to originate FHA loans out of its Mobile, Alabama branch." These points are sufficiently set forth in the record to support the circuit court's order.

[2] The McGehees allege that the $133.50 "interim interest" and the $59.50 "tax service fee" that make up the balance of the prepaid finance charges are also points. We express no opinion on whether these items

Section 5-19-4(g) provides:

> "Notwithstanding the provisions of this or any other section of this chapter, a creditor may, pursuant to contract, in a consumer loan or consumer credit sale secured by an interest in real property, charge and collect points in an amount not to exceed five percent of the original principal balance in the case of a closed-end loan or credit sale, or five percent of the total line of credit in the case of an open-end credit plan. Points may be paid in cash at the time of the loan or credit sale, or may be deducted from the proceeds and included in the original principal balance. Points shall be in addition to all other charges and are fully earned on the date of the loan or credit sale and may be excluded from the finance charge for the purpose of computing the finance charge refund."

(Emphasis added.)

Section 5-19-31(a) provides:

> "*The provisions of this chapter*, except the provisions of subdivision (1) of Section 5-19-1 and Section 5-19-3, *shall not apply to any loan*, forbearance, credit sale, lease, or other transaction involving an interest in real property or the sale, lease, or mortgage of an interest in real property, *where the creditor is a lending institution which is an approved mortgagee under the provisions of the National Housing Act* or is exempt from licensing under this chapter, or to any other loan, forbearance, credit sale, lease, or other transaction that is not a consumer transaction or to any transaction by a trust institution as defined in Section 5-12A-1(1), in its

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constitute points; if they do, the points in this loan exceed 8.5% of the amount financed.

capacity as a fiduciary under any plan or agreement qualified under 26 USC 401(a) or defined by 5 USC 8437, 26 USC 403(b) or 26 USC 457 or a trust exempt under 26 USC 501."

(Emphasis added.)[3]

The McGehees filed an action against UCLC alleging, in pertinent part:

"54. On or around June 21, 1991, the Defendants falsely represented to Plaintiffs that Defendant United Companies Lending Corporation is an approved mortgagee under the National Housing Act and further that Defendant UCLC is not governed by the provisions of Alabama's consumer protection law, Alabama Code § 5-19-1 et seq., commonly known as the 'Mini-Code.' Said representations were false, and at the time of the McGehee loan transaction Defendants knew that they were false and made them with the purpose of deceiving Plaintiffs and inducing Plaintiffs into entering into an unlawful loan transaction. The McGehee transaction was not made pursuant to the National Housing Act and was and is not a National Housing Act loan. On June 21, 1991, the date of the McGehee loan transaction made the basis of this lawsuit, Defendant United Companies Lending Corporation was not an approved mortgagee under the terms of the National Housing Act, and Defendants knew that Defendant UCLC's branch office at 857-A Downtowner Boulevard, Mobile, Alabama 36609, was not an approved branch under the National

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[3] Before a 1994 amendment, § 5-19-31(a) read: "None of the provisions of this chapter ... shall apply"; this opinion uses the current version because the change is insubstantial. See 1989 *Ala. Acts*, Act No. 89-541, p. 1132; 1994 *Ala. Acts*, Act No. 94-118, p. 146.

Housing Act. Many months prior to June 21, 1991, the date of the loan transaction made the basis of this lawsuit, Defendants ceased making any National Housing Act loans, and were not making any National Housing Act loans in Alabama or elsewhere at any time material to the instant action. Defendants never applied for nor received National Housing Act Mortgagee approval status for Defendant UCLC's branch office located at 857-A Downtowner Boulevard, Mobile, Alabama 36609.

"55. Defendants also falsely represented to Plaintiffs in the McGehee transaction that Defendant UCLC could lawfully charge points in excess of 5% of the original principal balance of the McGehee loan. Defendants further falsely represented to Plaintiffs during the loan closing on June 21, 1991 that everything regarding the McGehee transaction would be 'okay.' Said representations of material facts regarding the McGehee loan transaction were false and Defendants knew that they were false at the time of the McGehee transaction, and Plaintiffs justifiably relied upon said misrepresentations in entering into the loan made the basis of this lawsuit.

"56. Defendants intentionally concealed material facts from Plaintiffs about the McGehee loan transaction which Defendants had a duty to disclose to Plaintiffs. Specifically, Defendants failed to tell Plaintiffs that Defendant UCLC was in fact not an approved mortgagee under the National Housing Act, that Plaintiffs were and are in fact entitled to the protection of Alabama's consumer protection law known as the 'Mini-Code', and further that Defendant UCLC had no right to charge and/or collect 'points' from Plaintiffs in an amount in excess of

5% of the original principal balance of the McGehee loan.

"57. The aforesaid actions by Defendants constitute conscious and deliberate oppression, fraud, wantonness, and/or malice perpetrated upon the Plaintiffs. Neither of the Plaintiffs knew or through reasonable diligence could have known of the fraudulent, unlawful and wrongful conduct and activities perpetrated upon them described herein until Plaintiffs were informed of said wrongful conduct of Defendants herein on or around the latter part of August or the first part of September, 1993 by the undersigned counsel for the Plaintiffs. Plaintiffs are uneducated, unsophisticated, do not have high school diplomas, and did not realize until late August or September of 1993 that the loan made the basis of the McGehee transaction violated Alabama Code § 5-19-4(g). Defendants misled Plaintiffs and concealed the fraud and other wrongful conduct perpetrated upon Plaintiffs described herein by forcing Plaintiffs to sign the piece of paper attached hereto as Exhibit D entitled 'Acknowledgment by Applicant for Real Estate Loan.' Defendants falsely represented to Plaintiffs in Exhibit D that Defendant UCLC is not governed by Alabama Code § 5-19-4(g) to keep Plaintiffs from discovering the fraud and other wrongs perpetrated upon them."

UCLC raised as a defense and as a ground for summary judgment the exemption stated in § 5-19-31(a). The McGehees responded with a motion for summary judgment in their favor as to UCLC's exemption defense. The circuit court denied UCLC's motion and granted the McGehees' motion. This Court allowed an appeal pursuant to Rule 5, Ala. R. App. P.

The Department of Housing and Urban Development ("HUD") has promulgated regulations to effectuate the provisions of the National Housing Act ("NHA"). See 24 C.F.R. Part 202 (1994); Part 202 consists of §§ 202.1 through 202.20. Section 202.11(a) reads, in pertinent part:

> "(a) *Approval.* (1) A mortgagee may be approved for participation in the mortgage insurance programs authorized by the National Housing Act ... upon filing a request for approval on a form prescribed by the Secretary and signed by the applicant. ... Approval of the application by the Secretary shall constitute:
>
> "(i) The Secretary's agreement that the mortgagee shall be considered an approved mortgagee except as otherwise ordered by the Mortgagee Review Board, or an officer or subdivision of the Department of Housing and Urban Development to which the Mortgagee Review Board has delegated its power, unless the mortgagee voluntarily relinquishes its approval;
>
> "(ii) The mortgagee's agreement to comply at all times with the General approval requirements of § 202.12, and the special requirements for the class of mortgagee, at §§ 202.13, 202.14, 202.15, 202.16, or 202.17, for which it was approved; and
>
> "(iii) An origination approval agreement under which approval to originate mortgages for insurance may be terminated as provided in paragraph (d) of this section....
>
> "....
>
> "(4) *Approval of mortgagees may be restricted to geographic areas designated by the Secretary or may be approved to operate on a nationwide basis.*"

(Emphasis added.)[4]

UCLC was approved on October 3, 1990, as a "nonsupervised mortgagee" (§202.14) for 1-4 family residences. The approval by HUD includes this restriction: " This approval covers the HUD Field Office Jurisdiction of New Orleans, Louisiana."

Under the HUD regulations, a mortgagee approved for a limited geographic area may originate NHA-insured mortgage loans from outside its approved area only by establishing branch offices that are themselves approved to submit applications for NHA insurance from the region in which the branch office is located:

> "(m) *Branch offices.* [An approved mortgagee] may, only upon approval by the Secretary, maintain branch offices for the submission of applications for mortgage insurance. The mortgagee shall remain fully responsible to the Secretary for the actions of its branch offices."

24 C.F.R. § 202.12(m).[5]

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[4] The dissent quotes other portions of the HUD regulations, but, as we read these regulations, most of them apply only to an approved mortgagee's home office or to approved branch offices. It appears that unapproved branch offices are not supervised by HUD. Thus, approved mortgagees who maintain branch offices but do not seek approval to make NHA loans from those offices apparently may run those offices with no concern for most of the federal regulations. Thus, we are concerned by the dissent's suggestion that a claim based on the activities of such a branch office should be dismissed out of hand on a motion for summary judgment.

[5] The dissent characterizes the language in § 202.12(m) concerning branch office approval as "permissive." The suggestion in footnote 15 of the dissent that such an office could originate NHA loans is contrary to the Federal regulations. However, branch office approval is *required* before such an office may submit NHA loan applications.

The Mortgagee Approval Handbook published by HUD[6] reiterates these requirements for approval of branch offices in each jurisdiction in which the mortgagee wishes to originate NHA- or HUD-insured loans. Chapter 2 gives the "Mortgagee Approval Requirements," and division 2-1 gives the "General Approval Requirements," including paragraph h, which reads in pertinent part as follows:

> "*Extraterritorial Authority*: [An approved mortgagee may] Participate in geographic areas that are approved by HUD.
>
> "(1) Main offices may participate in the jurisdiction of the local HUD Field Office where they are located.
>
> "(2) Branch offices may participate in the jurisdiction of the local HUD Field Office where they are located.
>
> "(3) Mortgagees wishing to do business in HUD Field Office jurisdictions other than the HUD Field Office jurisdiction where the approved main office or branch offices are located must request such permission by completing form HUD-92001K, Notification of Mortgagee Change.
>
> > "(a) This permission to do business is limited to HUD Field Office jurisdictions *in states contiguous to the state in which the approved main or branch offices are located*; and in the case of servicing, only to the extent that they are within 200 miles of the mortgaged property to be serviced or they provide toll-free or accept collect calls on servicing questions."

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[6] Publication 4060.1, October 1980, with all changes through #3, 12/29/86; this version was in effect when UCLC obtained approval for its home office and when it made the loan to the McGehees.

(Emphasis added.)

UCLC acknowledges that it has no approved Alabama branch office. There is no evidence that UCLC had sought permission under the Handbook's provision 2-l(h)(3)(a) to do NHA-related business outside Louisiana, and, even if it had, Alabama is not contiguous to Louisiana.

The only legislative purpose for exemption from the Mini-Code of mortgage loans by NHA-approved mortgagees that presents itself to us is the fact that HUD extensively regulates its approved mortgagees. However, the Mortgagee Approval Handbook lists extensive requirements for approved main and branch offices: yearly verification reports; experience and qualifications of employees, including branch office managers; staffing and facilities requirements; communications capability and responsibility; restrictions on escrow accounts; responsibility for originating and servicing mortgages in accordance with HUD requirements; and net worth requirements. Because UCLC's Mobile office is not an approved branch office, however, these requirements do not apply to that office, and they do not apply to any other offices it has in Alabama.

The McGehees' mortgage loan from UCLC is not an NHA-insured mortgage loan. Thus, the provisions of the NHA do not apply to their loan.

UCLC argues that its mortgagors in Alabama, including the McGehees, are protected by Federal laws, notably the Real Estate Settlement Procedures Act (RESPA), 12 U.S.C. § 2601 et seq., and the Truth-In-Lending Act, 15 U.S.C. § 1601 et seq., so that the McGehees, UCLC says, are not left unprotected if UCLC is exempt from the Mini-Code. However, those Federal acts apply more broadly than to NHA-approved mortgagees, so the application of those acts is not a basis for exempting NHA-approved mortgagees from the protections given by the Mini-Code. Moreover, those Federal acts simply require disclosure and a three-day right of rescis-

sion; they do not set any limits on finance charges in general or points in particular.

For a discussion of the inadequacy of these disclosure and rescission requirements in protecting disadvantaged borrowers from predatory lending practices, including high discount points, see the testimony developed at a February 4, 1993, hearing before the House Subcommittee on Consumer Credit and Insurance. "Adding Injury to Injury: Credit on the Fringe." Hearing before the Subcommittee on Consumer Credit and Insurance of the Committee on Banking, Finance, and Urban Affairs, House of Representatives, Feb. 4, 1993, Serial No. 103-3. Witnesses and several members of the subcommittee expressed opinions that disclosure and rights of rescission do not provide enough protection, because many mortgages other than purchase-money mortgages do not require disclosure of annual percentage rates; because victims of targeted predatory practices are often working people who are less educated and less sophisticated about reading such instruments; and because the lenders start with small percentages of a homeowner's equity and later renew the loan, capitalizing accrued interest and thereby increasing the balance and the payment beyond the mortgagor's ability to pay. The description of predatory practices was summarized by Steven D. Caley of the Atlanta Legal Aid Society, Inc., whose prepared testimony includes the following:

> "Four principal conditions have combined to encourage unscrupulous lenders to defraud or mislead homeowners, particularly elderly, low income and unsophisticated homeowners who typically reside in redlined areas of their communities. The numerous schemes and devices utilized by these companies have been developed with the specific intent of ensnaring unsuspecting homeowners into signing loan papers with egregiously high interest rates, discount points, and other charges that the homeowners can never hope to repay so that the

lenders can ultimately obtain the equity in the home through foreclosure proceedings. The four principal conditions follow.

"First, the homes have high equity. Homeowners have acquired high equity in their homes either through appreciation, which has occurred at an extraordinarily high rate in the last 10 years (particularly in the sunbelt area), or by simply paying most or all of the mortgage on the home.

"Second, many states deregulated usury limits on mortgages in the early 1980s in response to skyrocketing interest rates of the late 1970s. Many states have no interest limits at all and many who do, have extremely high limits such as Georgia which has a five percent per month or sixty percent limit per year. Additionally many states do not regulate mortgage lenders, mortgage brokers or home improvement companies who are often part of the schemes which will be described below.

"Third, banks have redlined significant portions of their communities. When consumers no longer have access to conventional lenders for loans at reasonable rates of interest, they have no one else to turn to but the high rate lenders.

"Fourth, in some states such as Georgia, foreclosures are not supervised in any manner whatsoever. Georgia has no requirement that courts oversee foreclosures before, during, or after the sale in order to protect the homeowners' interest.

"In sum, homeowners with high equity values in their homes are the target of unscrupulous lenders who can charge any rate of interest they want to charge to homeowners who do not have access to credit from conventional lenders. These unprincipled lenders have basically placed themselves in a

win-win situation. If the homeowner pays the outrageous amounts, the lender reaps an enormous profit. If the homeowner is unable to pay, the lender forecloses and gets the house with equity typically in the tens of thousands of dollars.

"The above conditions have led to many abuses. The primary abuse has been the aggressive marketing of high interest, high prepaid finance charge mortgage loans to tens of thousands of low and moderate income homeowners who are mostly minority, elderly citizens. This practice has continued unabated for at least ten years. The loans typically carry prepaid finance charges ranging from 10 to 35 points and annual interest rates of 18% to 29%. Many of the companies engaging in these practices employ fraud, deception, falsified applications and forged deeds. The mortgages also often contain atrociously high brokers fees,[7] padded closing costs, balloon payments which trigger foreclosures, and high prepayment penalties which make refinancing difficult, if not impossible. All too often, foreclosure is the end result. Indeed entities such as Fleet Finance, Inc. have exceedingly high foreclosure rates (at least 10 times higher than the national average). It is thus clear that these lenders focus on the equity in the house, not the ability of the homeowner to repay the loan. Not only do families lose their homes which often represent a lifetime investment, but neighborhoods are destabilized, leading to drugs and crime."

Hearing, *op. cit.*, pp. 66-68.

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[7] See *Smith v. First Family Financial Services, Inc.*, 626 So. 2d 1266 (Ala. 1993), regarding an attempt to avoid the 5% discount point cap of § 5-19-4(g) by not disclosing commissions to mortgage brokers as prepaid finance charges.

The discount points and the conduct alleged against UCLC do not rise to the level described in this testimony, but the testimony serves to show the danger of allowing mortgage lenders that are not regulated except by the disclosure and rescission requirements of the Truth-In-Lending Act and RESPA to charge interest rates and discount points with no caps. Because UCLC's Alabama offices are not approved by HUD, they are not regulated by HUD. This fact supports a construction that only mortgagees whose offices in Alabama are approved by HUD are exempted by § 5-19-31 from the provisions of the Mini-Code. Such a construction would allow the points cap of § 5-19-4(g) to apply to such unregulated mortgagees and would provide at least that much protection to mortgagors taking loans from such mortgagees.

As to a broad category of "federally related mortgage loans," see 12 U.S.C. § 1735f-5(b),[8] Congress has enacted as part of the Depository Institutions Deregulation Monetary Control Act (DIDMCA), P.L. 96-221, Mar. 31, 1980, 94 Stat. 132, provisions limiting the application of state usury laws. *Id.*, Title V, § 501, codified at 12 U.S.C. § 1735f-7a (1988). Section 1735f-7a(b)(4), however, allows states, after March 31, 1980, *to limit discount points* on federally related mortgage loans.[9]

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[8] An NHA-insured mortgage loan is "federally related" as defined in § 1735f-5(b)(2)(B). Categories (A), (C), and (D) are "federally related" otherwise than by NHA insurance. Category (D) appears to be the broadest, making a loan "federally related" simply because the creditor "makes or invests in residential real estate loans aggregating more than $1,000,000 per year."

[9] 12 U.S.C. § 1735f-7a(b)(2) allowed states to override DIDMCA's preemption of state usury laws by enacting *interest rate* caps, but only within a narrow time period (1980-83) and only by expressly overriding DIDMCA. 12 U.S.C. § 1735f-7 more broadly allows states to override the usury law preemption that is specific to NHA loans. See *Doyle v. Southern Guar. Corp.*, 795 F.2d 907, 914 (11th Cir. 1986), which discusses these override provisions. These provisions are separate from

Section 5-19-4(g) of the Alabama Code was enacted in 1988 and therefore qualifies as an overriding exception to DIDMCA's preemption of state usury laws in regard to federally related mortgage loans. The United States District Court for the Southern District of Alabama has so held, rejecting a claim *by this same lender, UCLC*, that the points cap of § 5-19-4(g) cannot apply to its mortgage loans because that cap is preempted by DIDMCA. *Autrey v. United Companies Lending Corp.*, 872 F. Supp. 925 (Ala. 1995). The court assumed, without deciding, that UCLC's loan to Autrey was "federally related" and held: "Because [DIDMCA] does not completely pre-empt Plaintiffs' Mini Code claims, which this Court so finds since *§ 5-19-4(g) qualifies under DIDMCA's [§ 1735f-7a](b)(4) override exception*, remand is appropriate." 872 F. Supp. at 928 (emphasis added). Because Congress broadly allowed states to override its preemption of state usury laws *as to discount points*, we see no reason to limit the override enacted by our legislature in 1988 and codified at § 5-19-4(g).

Thus, we see no rational basis for extending to UCLC's offices in Alabama, which are not approved or regulated branch offices under the NHA approval procedures, the exemption by § 5-19-31(a) of mortgage loans made by NHA-approved mortgagees. There are overwhelming reasons, as described above, for construing that exemption not to apply to branch offices that are not approved to make NHA-insured loans.

The Mini-Code was enacted for consumer protection and so should be construed to effectuate that purpose, see, e.g., *Jackson v. CIT Group/Sales Financing, Inc.*, 630 So. 2d 368 (Ala. 1993); *Spears v. Colonial Bank of Alabama*, 514 So. 2d 814 (Ala. 1987); *Edwards v. Alabama Farm Bureau Mut.*

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§ 1735f-7a(b)(4), discussed in the text, which allows states to override DIDMCA preemption as to caps on *discount points* simply by enacting a cap on discount points after March 31, 1980. See *Autrey v. UCLC*, discussed later in the text.

Cas. Ins. Co., 509 So. 2d 232 (Ala. Civ. App. 1986), *cert. quashed*, 509 So. 2d 241 (Ala. 1987); *Derico v. Duncan*, 410 So. 2d 27 (Ala. 1982).

Because the Mini-Code was intended to provide protection to the public by regulating creditors, it should be construed so as to effectuate that public protection. "Statutes intended for the public benefit are to be construed most favorably to the public." *St. Paul Fire & Marine Ins. Co. v. Elliott*, 545 So. 2d 760, 762 (Ala. 1989); *First Alabama Bank of Dothan v. Renfro*, 452 So. 2d 464, 467 (Ala. 1984); *Gant v. Warr*, 286 Ala. 387, 391, 240 So. 2d 353, 355 (1970); *Employers Ins. Co. v. Johnston*, 238 Ala. 26, 32, 189 So. 58, 63 (1939).

Furthermore, § 5-19-31(a) provides an exemption from the provisions of the Mini-Code and so should be construed strictly against the party seeking the exemption. Exceptions or provisos, which restrict the operation of a statute, "should be strictly construed, and ... only those subjects expressly restricted should be freed from the operation of the statute," *Pace v. Armstrong World Industries Inc.*, 578 So. 2d 281, 284 (Ala. 1991).

These principles favor extending the protection of § 5-19-4(g) to an Alabama mortgagor whose Alabama mortgagee is not regulated under the NHA approval procedures and limiting the exemption in § 5-19-31(a) to mortgagees approved to make NHA loans in Alabama.[10]

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[10] The dissent construes the exemption most favorably to the party seeking exemption. The principle that the legislature is presumed to know the applicable laws and Federal regulations leads us to conclude that the legislature was aware that branch offices in Alabama require separate approval and therefore intended that only such approved branch offices would be exempt, not, as the dissent would conclude, that the legislature intended to exempt all offices opened by mortgagees with NHA approval in some other state, whether or not the offices in this state are approved to make NHA loans.

UCLC concedes that it is not approved to make NHA loans in Alabama and that the McGehees' loan is not an NHA-insured loan. Its Mobile, Alabama, office, from which the McGehees' loan originated, is not an NHA-approved branch office, and UCLC does not have a branch office that is approved to make NHA loans in Alabama. We hold, therefore, that UCLC is not "a lending institution which is an approved mortgagee under the provisions of the National Housing Act" for purposes of the exemption provided by § 5-19-31(a), because, as to its operations in Alabama to which the Mini-Code might apply, UCLC is not such an "approved mortgagee." Thus, UCLC is not exempt from the provisions of the Mini-Code and § 5-19-4(g) applies to UCLC's loan to the McGehees. The circuit court correctly entered the partial summary judgment for the McGehees, correctly holding that UCLC is subject to the points cap of § 5-19-4(g), and it correctly denied UCLC's motion for summary judgment on the McGehees' complaint alleging that their loan violates § 5-19-4(g), which allows a creditor to "charge and collect points in an amount not to exceed five percent of the original principal balance."

APPLICATION GRANTED; OPINION WITHDRAWN; OPINION SUBSTITUTED; AFFIRMED.

Almon, Shores, Kennedy, Cook, and Butts, JJ., concur.

Hooper, C. J., and Maddox and Houston, JJ., dissent.

HOUSTON, JUSTICE (dissenting).

The sole issue raised by the McGehees on their application for rehearing is whether the trial court erred in rejecting an alternative argument allegedly made by them, which they argue supported the partial summary judgment entered for them as to the applicability of the Ala. Code 1975, § 5-19-31 (a), exemption; we had reversed that partial summary judgment in our original opinion.[11] The McGehees argue that the trial court properly held that United Companies Lending Corporation (UCLC) was not entitled to a § 5-19-31(a) exemption, because they assert that their rejected alternative argument supports the partial summary judgment. The McGehees argue that the trial court erred in holding that UCLC was "an approved mortgagee under the provisions of the National Housing Act."[12] They concede that UCLC had received approval from the Secretary of Housing and Urban Development to underwrite federally insured loans out of its Baton Rouge, Louisiana, main office, but argue that, because UCLC did not obtain "branch office" approval for its Mobile, Alabama, office from the Mobile field office of the Department of Housing and Urban Development (hereinafter referred to as "HUD"), UCLC is not actually an NHA-approved mortgagee for purposes of § 5-19-31(a).[13] In

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[11] The issue the majority addresses in its opinion on rehearing was not raised by the McGehees in the trial court. The only issues raised below were addressed in my opinion of March 22, 1996.

[12] In its order granting the partial summary judgment for the McGehees, the trial court stated that "it is undisputed that [UCLC] is an approved mortgagee under the provisions of the National Housing Act."

[13] The pertinent portion of § 5-19-31(a) (as it read before the February 24, 1994, amendment) states:

> "None of the provisions of this chapter ...shall apply to any ...mortgage of an interest in real property, where the creditor is a lending institution which is *an approved mortgagee under the provisions of the National Housing Act....*"

(Emphasis added.)

order to resolve the issue raised by the McGehees -- whether HUD approval to make federally insured loans in Alabama is a prerequisite to obtaining a § 5-19-31(a) exemption -- this Court should have looked to federal law, which clearly establishes that UCLC is a HUD-approved mortgagee regardless of whether it seeks "branch approval" for any of its local offices. Because the majority did not, I must respectfully dissent.

Federal law gives the Secretary of Housing and Urban Development the authority to promulgate regulations governing the approval of lending institutions for participation as mortgagees in federal mortgage insurance programs:

> "*The Secretary [of Housing and Urban Development is authorized*, upon application by the mortgagee, to insure as hereinafter provided any mortgage offered to him which is eligible for insurance as hereinafter provided, and, *upon such terms as the Secretary may prescribe, to make commitments for the insuring of such mortgages prior to the date of their execution or disbursement thereon.*"

12 U.S.C. § 1709(a). (Emphasis added.) Furthermore, 12 U.S.C. § 1709(b)(1) states:

> "To be eligible for insurance ... a mortgage shall --
>
> > "(1) Have been made to, and be held by, a mortgagee approved by the Secretary as responsible and able to service the mortgage properly."

In order to fulfill the mandate of § 709(a) that the Secretary of Housing and Urban Development prescribe terms for "mak[ing prior] commitments for the insuring of ... mortgages," HUD has promulgated regulations setting out the criteria of a federally insurable mortgage and the requirements for being "a mortgagee approved by the Secretary" under 12 U.S.C. § 1709(b)(1).

The regulations pertinent to the issue before us -- whether UCLC was "a mortgagee approved by the Secretary," 12 U.S.C. § 1709(b)(1), when it made the McGehee loan -- are contained in subpart B of part 202 of title 24 of the Code of Federal Regulations. The first pertinent provision is 24 C.F.R. § 202.11(a), which states:

> "(a) *Approval.* (1) A mortgagee may be approved for participation in the mortgage insurance programs authorized by the National Housing Act, except Title I of the Act, upon filing a request for approval on a form prescribed by the Secretary and signed by the applicant. The approval form shall be accompanied by such documentation as may be prescribed by the Secretary to support the request for approval."

The McGehees do not dispute the fact that UCLC filed an application and the necessary accompanying documents, as required by § 202.11(a) before making the McGehee loan.

The additional requirements for being an approved mortgagee for participation in federally insured loan programs are contained in 24 C.F.R. § 202.12:

> "To be approved for participation in the mortgage insurance programs authorized by the National Housing Act, except Title I of the Act, and to maintain approval, a mortgagee shall meet the general requirements of this section ... and the specific requirements of § 202.13 through § 202.19, as appropriate.
>
> "(a) *Business form.* It shall be a corporation or other chartered institution, a permanent organization having succession or a partnership ....
>
> "....
>
> "(b) *Employees.* It shall employ competent personnel ... and adequate staff and facilities to

originate and service mortgages in accordance with applicable regulations, to the extent the mortgagee engages in such activities.

"(c) *Officers.* All employees who will sign applications for mortgage insurance on behalf of the mortgagee shall be corporate officers or shall otherwise be authorized to bind the mortgagee ....

"(d) *Escrows.* It shall not use escrow funds for any purpose other than that for which they were received....

"(e) *Related laws.* It shall comply with the provisions of the Fair Housing Act, Executive Order 11063, Equal Credit Opportunity Act, the Real Estate Settlement Procedures Act of 1974, and all other Federal laws relating to the lending or investing of funds in real estate mortgages.

"(f) *Servicing.* It shall comply with the servicing responsibilities contained in subpart C of part 203 and in part 207, and with all other applicable regulations....

"(g) *Business changes.* It shall provide prompt notification ...of all changes in its legal structure

"(h) *Reports.* It shall file the following reports, records and documentation:

"....

"(i) *Financial statements.* It shall, upon request by the Secretary, submit a copy of its latest financial statement, submit such information as the Secretary may request, and submit to an examination of that portion of its records which relates to its insured mortgage activities.

"(j) *Quality control plan.* It shall implement a written Quality Control Plan ...that assures compli-

ance with the regulations and other issuances of the Secretary....

"(k) *Fees.* A mortgagee ...shall pay an application fee and annual fees ....

"(l) *Ineligibility.* ...[N]either the applicant mortgagee nor any officer, partner, director, principal or employee of the applicant mortgagee shall:

"(1) Be suspended, debarred or otherwise restricted under ...this title, or under similar procedures of any other Federal agency;

"(2) Be indicted for, or have been convicted of, an offense which reflects upon the responsibility, integrity or ability of the mortgagee to be an approved mortgagee;

"(3) Be subject to unresolved findings ...; or

"(4) Be engaged in business practices that do not conform to generally accepted practices of prudent mortgagees or that demonstrate irresponsibility.

"(m)*Branch offices.* It may, only upon approval of the Secretary, maintain branch offices for the submission of applications for mortgage insurance. The mortgagee shall remain fully responsible to the Secretary for the actions of its branch offices.

"(n) *Net worth.* It shall have and maintain a net worth, in assets acceptable to the Secretary, of the following amounts.

"[The listing of amounts is omitted.]

"(o) *Effective date* [of the net worth provisions].

"(p) *Conflict of interest.* ...The mortgagee shall not pay a referral fee to any person or organization.

> "(q) *Liquid assets.* It shall maintain liquid assets consisting of cash or its equivalent acceptable to the Secretary in the amount of 20 percent of its net worth, up to a maximum liquidity requirement of $100,000.
>
> "(r) *Fidelity bond.* ...[T]he mortgagee shall maintain fidelity bond coverage and errors and omissions insurance acceptable to the Secretary and in an amount required by the Secretary ...."

Last, because UCLC falls within the § 202.14(a) definition of a "nonsupervised mortgagee," UCLC must, in addition to complying with the above regulations, also comply with additional, more specific rules contained in § 202.14(c) as to the maintenance of warehouse lines of credit and the filing of audit reports.[14]

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[14] I cannot agree with the following assertion of the majority:

> "Because UCLC's Alabama offices are not approved by HUD, they are not regulated by HUD. This fact supports a construction that only mortgagees whose offices in Alabama are approved by HUD are exempted by § 5-19-31 from the provisions of the Mini-Code."

___ So.2d at ___. The McGehees and all other persons who do business with mortgage companies that are NHA-approved mortgagees do benefit from the regulations contained in 24 C.F.R. §§ 202.12 and 202.14, whether or not the office they deal with is a "branch office" approved under § 202.12(m). These regulations ensure that NHA-approved mortgagee institutions are reputable and financially stable, and, most importantly, that such institutions are capable of answering to the mortgagor if a problem arises (in other words, compliance with these regulations ensures that a mortgagee is not a "fly-by-night" mortgage company). For example, the regulations applicable to all NHA-approved mortgagees require that such mortgagees: follow procedures acceptable in the mortgage industry generally (see § 202.12(l)(4)), have adequate financial resources (see § 202.12(n), (o), and (q)), are insured for errors and omissions (see § 202.12(r)), as well as comply with federal lending and housing laws.

The McGehees contend that UCLC failed to comply with § 202.12(m) and, therefore, was not "an approved mortgagee under the provisions of the National Housing Act" when it made its loan to them. That subsection states:

> "(m) *Branch offices.* It may, only upon approval of the Secretary, maintain branch offices for the submission of applications for mortgage insurance...."

The McGehees argue that UCLC's Mobile office was a "branch office" that must have been registered with the HUD field office in Mobile in order to comply with § 202.12. I cannot agree with their contention though, because the plain language of subsection (m) does not require the approval of any lending institution office that does not "submi[t] ...applications [to HUD] for mortgage insurance." It is undisputed that UCLC has never made or underwritten a single federally insured loan out of its Mobile office. Furthermore, subsection (m) is written in permissive language ("may ...maintain [approved] branch offices"). It does not require that UCLC or any other NHA-approved mortgagee open "branch offices" at all.[15]

In the alternative, the McGehees argue that we should construe § 5-19-31(a) to require more than 24 C.F.R. §§ 202.11 and 202.12 require to be an NHA-approved mortgagee. Their argument for the judicial imposition of an additional Alabama approval requirement on mortgagees seeking a § 5-19-31(a) exemption is very similar to the McGehees' argument that we rejected in our original opinion -- that this Court should, for the same policy reasons, construe the § 5-

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[15] UCLC also argued in its brief that, according to its reading of the regulations, it would not have violated 24 C.F.R. §202.12(m) for its Mobile office to go as far as to take applications for federally insured mortgages without "branch office" approval, as long as its Mobile office was not participating in the underwriting of federally insured mortgages.

19-31(a) exemption to apply only in instances where an NHA-approved mortgagee is actually making a federally insured mortgage. The majority seems to base its opinion on rehearing on the same sort of policy argument:

> "Thus, we see no rational basis for extending to UCLC's offices in Alabama, which are not approved or regulated branch offices under the NHA approval procedures, the exemption by § 5-19-31(a) of mortgage loans made by NHA-approved mortgagees."

_____ So.2d at _____. See also note 3. The problem with the reasoning underlying the McGehees' argument and the majority's opinion is that it fails to acknowledge that Alabama courts cannot resort to judicial construction of a statutory provision unless the provision in question is ambiguous.[16] After fully considering the statutory language in question, I cannot conclude that the § 5-19-31(a) phrase "an approved mortgagee under the provisions of the National Housing Act" is ambiguous. That phrase clearly and unambiguously leads the reader to the Federal law, contained in 24 C.F.R. §§ 202.11(a) and 202.12, defining which mortgagees are, and which are not, approved to make NHA federally insured mortgages.

But even if the § 5-19-31(a) phrase "an approved mortgagee under the provisions of the National Housing Act" could be held ambiguous, I could not agree with the majority's contention that this Court should interpret that phrase as requiring NHA-approved mortgagees to seek "branch office"

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[16] See *Hines v. Riverside Chevrolet-Olds, Inc.*, 655 So.2d 909, 924 (Ala. 1994), which states:

> "When a statutory pronouncement is clear and not susceptible to different interpretations, it is a paramount judicial duty to abide by that clear pronouncement."

(Citing *Macon v. Huntsville Utilities*, 613 So.2d 318 (Ala. 1992).)

approval in Alabama in order to qualify for a § 5-19-31(a) exemption. "It is a fundamental principle of statutory construction that [a court construing a statute will assume that] in enacting the statute the legislature had full knowledge and information as to prior and existing law ...on the subject of the statute." *Miller v. State*, 349 So.2d 129, 131 (Ala.Crim.App. 1977).[17] "[W]e presume that the Legislature knows the meaning of the words it uses in enacting legislation."

Ex parte Jackson, 614 So.2d 405, 407 (Ala. 1993). In construing the phrase in question, this Court must presume that the legislature had full knowledge of the NHA approval procedures contained in the federal regulations. Those regulations, as shown above, provide that a mortgagee that wishes to make federally insured mortgages must first seek HUD approval for its main underwriting office, and that once the mortgagee is approved by the Secretary of HUD it can then seek approval for any other "branch offices" out of which the approved mortgagee intends to underwrite federally insured

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[17] See *Holstein v. Norandex, Inc.*, 194 W. Va. 727, 461 S.E.2d 473, 477 (1995):

> "A statute should be so read and applied as to make it accord with the spirit, purposes and objects of the general system of law of which it is intended to form a part; *it being presumed that the legislators who drafted and passed it were familiar with all existing law. applicable to the subject matter, whether constitutional, statutory or common, and intended the statute to harmonize completely with the same* and aid in the effectuation of the general purpose and design thereof, if its terms are consistent therewith."

(Emphasis added.) (Quoting *State ex rel. Goff v. Merrifield*, 191 W.Va. 473, 446 S.E.2d 695 (1994), and other cases.) See also *Holmes County School Bd. v. Duffell*, 651 So.2d 1176 (Fla. 1995); *Wilson v. Miles*, 218 Ga. App. 806, 463 S.E.2d 381 (1995); *Nunnally v. State Dep't of Public Safety*, 663 So.2d 254 (La. App. 1995); *Smith v. Retirement Bd.*, 656 A.2d 186 (R.I. 1995); *Still v. First Tennessee Bank, N.A.*, 900 S.W.2d 282 (Tenn. 1995).

mortgages .[18] Section 202.12(m) makes it abundantly clear that "branch office" approval is not a requirement for being an NHA-approved mortgagee, but is instead completely optional.[19]

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[18] For the same reasons, this Court must also presume that the legislature was aware that 24 C.F.R. § 202.11(a)(4) allows the Secretary of HUD to restrict geographically the approval of mortgagees applying under § 202.11(a). Subsection (a)(4) states:

> "(4) Approval of mortgagees may be restricted to geographic areas designated by the Secretary or may be approved to operate on a nationwide basis."

Had the legislature intended to restrict the application of Ala. Code 1975, § 5-19-31(a), to NHA-approved mortgagees who have been approved to make federally insured loans in Alabama, the legislature could have easily done so, just as the legislature, if it had so chosen, could have restricted the application of the exemption to federally insured mortgage loans only (an argument rejected in this Court's original opinion). See *Ex parte Jackson*, 614 So.2d 405, 407 (Ala. 1993):

> "[W]e presume that the Legislature knows the meaning of the words it uses in enacting legislation. ... [I]f it intended [the section in question] to apply in this case, [it] knew how to draft a statute to reach that end.... *The judiciary will not add that which the Legislature chose to omit.*"

(Emphasis added.)

[19] The requirements for being an NHA-approved mortgagee, aside from the § 202.11(a) application requirement, are contained in 24 C.F.R. § 202.12. That section states:

> "To be approved for participation in the mortgage insurance programs authorized by the National Housing Act, except Title I of the Act, and to maintain approval, a mortgagee shall meet the general requirements of this section ... and the specific requirements of § 202.13 through § 202.19, as appropriate."

(Emphasis added.) The requirement at issue here is found in subpart (m):

> "(m) *Branch offices.* It may, only upon approval by the Secretary, maintain branch offices for the submission of applications for mortgage insurance. The mortgagee shall remain

I cannot conclude, from the facts contained in the record, that UCLC failed to satisfy any of the federal requirements found in 24 C.F.R. §§ 202.11, 202.12, or 202.14 for being approved to participate in the mortgage insurance programs authorized by the National Housing Act; therefore, I must dissent, because I am convinced that our initial holding -- that the trial court erred in entering the partial summary judgment in favor of the McGehees as to the issue of the applicability of the Ala. Code 1975, § 5-19-31(a), exemption -- was correct.

Hooper, C. J., and Maddox, J., concur.

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fully responsible to the Secretary for the actions of its branch offices."

D-1

IN THE SUPREME COURT OF ALABAMA

December 6, 1996

1941234

United Companies Lending Corporation v. Michael McGehee, et al.

(Mobile: CV-93-1961)

NOTICE

The application for rehearing filed in this cause on October 25, 1996, is overruled. No opinion written on rehearing.

PER CURIAM - Almon, Shores, Kennedy, Cook and Butts, JJ., concur;

Hooper, CJ., Maddox and Houston, JJ., dissent.

CODE OF ALABAMA 1975

TITLE 5. BANKS AND FINANCIAL INSTITUTIONS.

CHAPTER 19. CONSUMER FINANCE

§ 5-19-4 Additional charges for default or deferral; prepayment; renewal or refinancing; and real property transactions.

* * *

(g) Notwithstanding the provisions of this or any other section of this chapter, a creditor may, pursuant to contract, in a consumer loan or consumer credit sale secured by an interest in real property, charge and collect points in an amount not to exceed five percent of the original principal balance in the case of a closed-end loan or credit sale, or five percent of the total line of credit in the case of an open-end credit plan. Points may be paid in cash at the time of the loan or credit sale, or may be deducted from the proceeds and included in the original principal balance. Points shall be in addition to all other charges and are fully earned on the date of the loan or credit sale and may be excluded from the finance charge for the purpose of computing the finance charge refund.

* * *

§ 5-19-31 Nonapplicability of chapter to certain transactions; certain laws not repealed or amended; intent of section.

(a) The provisions of this chapter, except the provisions of subdivision (1) of Section 5-19-1 and Section 5-19-3, shall not apply to any loan, forbearance, credit sale, lease, or other transaction involving an interest in real property or the sale, lease, or mortgage of an interest in real property, where the creditor is a lending institution which is an approved mortgagee under the provisions of the National Housing Act or is exempt from licensing under this chapter, or to any other loan, forbearance, credit sale, lease, or other transaction that is not a

consumer transaction or to any transaction by a trust institution as defined in Section 5-12A-1(1), in its capacity as a fiduciary under any plan or agreement qualified under 26 USC 401(a) or defined by 5 USC 8437, 26 USC 403(b) or 26 USC 457 or a trust exempt under 26 USC 501.

* * *

CODE OF FEDERAL REGULATIONS

TITLE 24 – HOUSING AND URBAN DEVELOPMENT

SUBTITLE B – REGULATIONS RELATING TO HOUSING AND URBAN DEVELOPMENT

CHAPTER II – OFFICE OF ASSISTANT SECRETARY FOR HOUSING – FEDERAL HOUSING COMMISSIONER, DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

SUBCHAPTER B – MORTGAGE AND LOAN INSURANCE PROGRAMS UNDER NATIONAL HOUSING ACT AND OTHER AUTHORITIES

PART 202 – APPROVAL OF LENDING INSTITUTIONS AND MORTGAGES

SUBPART B – APPROVAL OF MORTGAGEES

§ 202.10 Definitions

As used in this subpart:

(a) Mortgage means a mortgage as defined in this chapter, or a loan authorized for insurance under Title II of the National Housing Act;

(b) Mortgagee means a mortgage lender which meets the definition of either a supervised mortgagee at § 202.13, a non-supervised mortgagee at § 202.14, a loan correspondent at § 202.15, an investing mortgagee at § 202.16, or a governmental institution at § 202.17

§ 202.11 Approval, origination approval agreement, recertification, withdrawal of approval and termination of approval agreement.

(a) Approval.

(1) A mortgagee may be approved for participation in the mortgage insurance programs authorized by the National Housing Act, except Title I of the Act, upon filing a request for approval on a form prescribed by the Secretary and signed by the applicant. The approval form shall be accompanied by such documentation as may be prescribed by the Secretary to support the request for approval. Approval of the application shall constitute:

(i) The Secretary's agreement that the mortgagee shall be considered an approved mortgagee except as otherwise ordered by the Mortgagee Review Board, or an officer or subdivision of the Department of Housing and Urban Development to which the Mortgagee Review Board has delegated its power, unless the mortgagee voluntarily relinquishes its approval;

(ii) The mortgagee's agreement to comply at all times with the General approval requirements of § 202.12, and the special requirements for the class of mortgagee, at §§ 202.13, 202.14, 202.15, 202.16 or 202.17, for which it was approved; and

(iii) An origination approval agreement under which approval to originate mortgages for insurance may be terminated as provided in paragraph (d) of this section, in addition to any actions of the Mortgagee Review Board authorized by part 25 of this title.

(2) Approval may be restricted to participation in the home mortgage insurance programs or the multifamily mortgage insurance programs

(3) Separate approval is required under subpart A of this part for participation in the Title I Program, and additional ap-

proval is required for participation in the Title II Direct Endorsement program or for the Coinsurance Program as provided in § 203.3 or 24 CFR part 204.

(4) Approval of mortgagees may be restricted to geographic areas designated by the Secretary or may be approved to operate on a nationwide basis.

(5) A mortgagee approved under this subpart may, with the approval of the Secretary, designate another approved mortgagee approved under §§ 202.13 or 202.14 as authorized agent for the purpose of submitting applications for mortgage insurance in its name and on its behalf if:

(i) The property is located in an area determined by the Secretary to be under-served;

(ii) The mortgagee is approved as a supervised mortgagee under § 202.13 and the authorized agent is an affiliate or subsidiary of the mortgagee; or

(iii) The mortgagee is approved under § 202.17.

(b) Recertification of approval. On each anniversary of the approval of a mortgagee, the Secretary shall undertake a recertification procedure to determine whether continued approval is appropriate. The Secretary shall review the yearly verification report required by § 202.12(h)(2) and other pertinent documents, determine whether all application and annual fees which are due have been paid, and request any additional information needed to make a determination regarding continuation of approval. For each mortgagee which is approved before January 8, 1993, the recertification procedure on the first anniversary of approval occurring after January 8, 1993, shall include an origination approval agreement under which approval to originate mortgages for insurance may be terminated as provided in paragraph (d) of this section.

(c) Withdrawal and suspension of approval. Mortgagee approval may be suspended or withdrawn by the Mortgagee Review Board as provided in part 25 of this title.

(d) Termination of origination approval agreement--

(1) Definitions. For purposes of this paragraph (d):

(i) Normal rate for defaults and claims means the rate of defaults and claims on HUD insured mortgages for the geographic area served by a HUD field office, or other area designated by the Secretary, in which the mortgagee originates mortgages.

(ii) Defaults means insured mortgages in default for 90 or more days within one year after endorsement.

(iii) Claims means insured mortgages for which the Secretary pays an insurance claim within 18 months after endorsement.

(2) Review of defaults and claims. Every three months, the Secretary shall review the number of defaults and claims on mortgages originated by each mortgagee in the geographic area served by a HUD field office. The Secretary may also review the performance of a mortgagee's branch offices individually and may impose the sanctions provided for in this section on a branch as well as on a mortgagee as a whole.

(3) Termination.

(i) If a mortgagee has a rate of defaults and claims on insured mortgages originated in an area during the Federal fiscal year which was in excess of 200 percent of the normal rate, and in excess of the national default and claim rate for insured mortgages, the Secretary shall notify the mortgagee that its origination approval agreement shall be terminated 60 days after notice was given, without action by the Mortgagee Review Board except as provided in paragraph (d)(3)(iii) of this section. For this purpose, a mortgage is considered to be originated in the same Federal fiscal year in which it is endorsed for insurance.

(ii) Before the Secretary sends the termination notice the Secretary shall review the census tract area concentrations of the defaults and claims. If the Secretary determines that the excessive rate is the result of mortgage lending in under-

served areas the Secretary may determine not to terminate the approval agreement.

(iii) Prior to termination the mortgagee may request an informal conference with the Deputy Assistant Secretary for Single Family Housing or his or her designee. After considering relevant reasons and factors beyond the mortgagee's control that contributed to the excessive default and claim rates, the Deputy Assistant Secretary for Single Family Housing or designee may withdraw the termination notice and may place the mortgagee on credit watch status.

(4) Credit watch status. If a mortgagee has a rate of defaults and claims on insured mortgages originated in an area during a Federal fiscal year which was greater than 150 percent but equal to or less than 200% of the normal rate, the Secretary shall notify the mortgagee that it is being placed on credit watch status. For this purpose, a mortgage is considered to be originated in the same Federal fiscal year in which it is endorsed for insurance. Before the credit watch notice is sent the Secretary shall review the census tract area concentrations of the defaults and claims. If the Secretary determines that the excessive rate is the result of mortgage lending in underserved areas the Secretary may determine not to place the mortgagee on credit watch status.

(5) Effect of credit watch. Insured mortgages originated during a six month period from the date of the credit watch notice will be reviewed for excessive default rates. A mortgagee will be removed from credit watch status if the rate of defaults and claims for the six month tracking period decreases to 150 percent or less one year after that six month tracking period. The origination approval agreement for a mortgagee subject to credit watch may be terminated if the mortgagee's rate of defaults and claims on insured mortgages originated in an area during the six month tracking period is more than 150 percent of the normal rate one year after that six month tracking period. The Secretary shall provide 60

days notice and an opportunity for an informal conference as required by § 202.11(d)(3)(iii) to a mortgagee which will have its origination approval agreement terminated subsequent to a credit watch.

(e) Effects of termination of origination approval agreement. Termination of the origination approval agreement shall not affect:

(1) The Secretary's ability to insure eligible mortgages, absent fraud or misrepresentation, if the mortgagor and all terms and conditions of the mortgagee were approved before the termination by the Direct Endorsement mortgagee or by a firm commitment issued by the Secretary, but no other mortgages originated by the mortgagee shall be insured unless a new originated approval agreement is accepted by the Secretary.

(2) A mortgagee's obligation to continue to pay insurance premiums and meet all other obligations associated with insured mortgages;

(3) A mortgagee's right to reapply for a new origination approval agreement provided that the mortgagee is still an approved mortgage, the general approval requirements at 202.12 and the specific requirements of 203.13 through 202.19 continue to be met, and the Secretary determines that the underlying causes for termination have been satisfactorily remedied; or

(4) A mortgagee's right to purchase insured mortgages or to service its own portfolio or the portfolios of other mortgagees with which it has a servicing contract.

(Approved by the Office of Management and Budget under control number 2502-0005)

[58 FR 13537, March 12, 1993]

§ 202.12 General approval requirements.

To be approved for participation in the mortgage insurance programs authorized by the National Housing Act, except Ti-

tle I of the Act, and to maintain approval, a mortgagee shall meet the general requirements of this section (except as provided in § 202.17(b)) and the specific requirements of § 202.13 through § 202.19, as appropriate.

(a) Business form. It shall be a corporation or other chartered institution, a permanent organization having succession or a partnership. All partnerships must meet the requirements of paragraphs (a)(1) through (a)(4) if this section.

(1) Each general partner must be a corporation or other chartered institution consisting of two or more persons.

(2) One general partner must be designated as the managing general partner. The managing general partner shall comply with the requirements of paragraphs (b), (c) and (g) of this section. The managing general partner must have as its principal activity the management of one or more partnerships, all of which are mortgage lenders, and must have exclusive authority to deal directly with the Secretary on behalf of each partnership. Newly admitted partners must agree to the management of the partnership by the designated managing general partner. If the managing general partner shall be substituted, and the Secretary shall be immediately notified of the substitution.

(3) The partnership agreement shall specify that the partnership shall exist for the minimum term of years required by the Secretary. All insured mortgages held by the partnership shall be transferred to a HUD approved mortgagee prior to the termination of the partnership. The partnership shall specifically be authorized to continue its existence in the event that a partner withdraws.

(4) The Secretary must be notified immediately of any amendments to the partnership agreement which would affect the partnership's actions under any mortgage insurance program administered by the Secretary.

(b) Employees. It shall employ competent personnel trained to perform their assigned responsibilities, including origina-

tion, servicing and collection activities, and adequate staff and facilities to originate and service mortgages in accordance with applicable regulations, to the extent the mortgagee engages in such activities.

(c) Officers. All employees who will sign applications for mortgage insurance on behalf of the mortgagee nor any officer, partner, director, principal or employee of the mortgagee shall be corporate officers or shall otherwise be authorized to bind the mortgagee in matters involving the origination of mortgage loans.

(d) Escrows. It shall not uses escrow funds for any purpose other than that for which they were received. It shall segregate escrow commitment deposits, work completion deposits, and all periodic payments received under insured mortgages on account of ground rents, taxes, assessments, and insurance premiums, and shall deposit such funds with one or more financial institutions in a special account or accounts that are fully insured by the Federal Deposit Insurance Corporation or the National Credit Union Administration, except as otherwise provided in writing by the Secretary.

(e) Related laws. It shall comply with the provisions of the Fair Housing Act, Executive Order 11063, Equal Credit Opportunity Act, the Real Estate Settlement Procedures Act of 1974, and all other Federal laws relating to the lending or investing of funds in real estate mortgages.

(f) Servicing. It shall comply with the servicing responsibilities contained in subpart C of part 203 and in part 207, and with all other applicable regulations contained in this title 24, and with such additional conditions and requirements as the Secretary may impose.

(g) Business changes. It shall provide prompt notification, on a form prescribed by the Secretary, of all changes in its legal structure, including, but not limited to, mergers, terminations, name, location, control of ownership, and character of business.

(h) Reports. It shall file the following reports, records and documentation:

(1) Upon application for approval and with each annual recertification, a certification that the mortgagee had not been refused a license and has not been sanctioned by any State or States in which it will originate insured mortgages;

(2) A yearly verification report on a form prescribed by the Secretary;

(3) An audited or unaudited financial statement, within 30 days of the end of each fiscal quarter in which the mortgagee experiences an operating loss of 20 percent of its net worth, and until the mortgagee demonstrates an operating profit for two consecutive quarters or until the next recertification, whichever is the longer period; and

(4) A statement of net worth within 30 days of the commencement of voluntary or involuntary bankruptcy, conservatorship, receivership or any transfer of control to a Federal or State supervisory agency.

(i) Financial statements. It shall, upon request by the Secretary, submit a copy of its latest financial statement, submit such information as the Secretary may request, and submit to an examination of that portion of its records which relates to its insured mortgage activities.

(j) Quality control plan. It shall implement a written Quality Control Plan, acceptable to the Secretary, that assures compliance with the regulations and other issuances of the Secretary regarding mortgage origination and servicing.

(k) Fees. A mortgagee, other than one meeting the requirements of § 202.17, shall pay an application fee and annual fees, including additional fees for each branch office authorized to submit applications for mortgage insurance, in such amounts and at such times as the Secretary may require. The Secretary may identify classes or groups of mortgagees that are exempt from one or more of these fees.

(l) Ineligibility. At the time of application and at all times while approved as a mortgagee , neither the applicant mortgagee nor any officer, partner, director, principal or employee of the applicant mortgagee shall:

(1) Be suspended, debarred or otherwise restricted under part 24 or part 25 of this title, or under similar procedures of any other Federal agency;

(2) Be indicted for or have been convicted of, an offense which reflects upon the responsibility, integrity or ability of the mortgagee to be an approved mortgagee;

(3) Be subject to unresolved findings as a result of HUD or other governmental audits or investigations; or

(4) Be engaged in business practices that do not conform to generally accepted practices of prudent mortgagees or that demonstrate irresponsibility.

(m) Branch offices. It may, only upon approval by the Secretary, maintain branch offices for the submission of applications for mortgage insurance. The mortgagee shall remain fully responsible to the Secretary for the actions of its branch offices.

(n) Net worth. It shall have and maintain a net worth, in assets acceptable to the Secretary, of the following amounts.

(1) Supervised mortgagees under § 203.13 and non-supervised mortgagees under § 202.14, including sponsors of loan correspondents, shall have a net worth at least equal to $250,000, plus one percent of the volume of mortgages in excess of $25,000,000, up to a maximum required net worth of $1,000,000. Mortgage volume shall include insured mortgages originated, serviced, and purchased by the mortgagee in the preceding fiscal year of the mortgagee. To determine mortgage volume, the Secretary will add the aggregate original principal amount of the mortgages that were endorsed for insurance during the mortgagee's prior fiscal year and the aggregate principal amount of all insured mortgages serviced

except those that were originated by the mortgagee or purchased from its loan correspondent(s) by the mortgagee at the end of the mortgagee's prior fiscal year. The mortgage volume for loan sponsors shall also include the aggregate principal amount of mortgages purchased from its loan correspondent(s) during the mortgagee's prior fiscal year.

(2) Mortgagees approved for participation only in the multifamily mortgage insurance programs under § 202.11(a)(2) are required to have a net worth of at least $250,000.

(3) Mortgagees which are loan correspondents under § 202.15 shall have a net worth of at least $50,000 and at least an additional $25,000 net worth for each branch office of the loan correspondent up to a combined maximum required net worth of $250,000.

(4) Mortgages approved under §§ 202.16 and 202.17 are not required to maintain a specific net worth.

(o) Effective date. Mortgagees approved on or after January 8, 1993, shall be required to have a net worth as required by § 203.12(n) upon approval, except supervised and non-supervised mortgagees may have a net worth of $250,000 for the first year of approval. All mortgagees approved before January 8, 1993, must meet the net worth requirements of paragraph (n) of this section by January 9, 1995.

(p) Conflict of interest. A mortgagee may not pay anything of value, directly or indirectly, in connection with any insured mortgage transaction or transaction to any person or entity if such person or entity has received any other consideration from the mortgagor, seller, builder, or any other person for services related to such transactions or related to the purchase of sale of the mortgaged property, except that consideration as may be approved by the Secretary may be paid for services actually performed. The mortgagee shall not pay a referral fee to any person or organization.

(q) Liquid assets. It shall maintain liquid assets consisting of cash or its equivalent acceptable to the Secretary in the

amount of 20 percent of its net worth, up to a maximum liquidity requirement of $100,000.

(r) Fidelity bond. Except for loan correspondents, the mortgagee shall maintain fidelity bond coverage and errors and omissions insurance acceptable to the Secretary and in an amount required by the Secretary, or alternative insurance coverage approved by the Secretary, that assures the faithful performance of the responsibilities of the mortgagee.

(Approved by the Office of Management and Budget under control number 2502-0005)

§ 202.13 Supervised mortgagees.

(a) Definition. A supervised mortgagee is a financial institution which is a member of the Federal Reserve System or an institution whose accounts are insured by the Federal Deposit Insurance Corporation of the National Credit Union Administration.

(b) General functions. A supervised mortgagee may submit applications for mortgage insurance, and may purchase, hold, service or sell insured mortgages.

(c) Special requirement. In addition to the general approval requirements in § 202.12, a supervised mortgagee shall promptly notify the Secretary in the event of termination of its supervision by its supervising agency.

(d) Trust companies. Approval of a banking institution or a trust company as a supervised mortgagee shall constitute approval of such institution or company when lawfully acting in a fiduciary capacity in investing fiduciary funds which are under its individual or joint control. Upon termination of such fiduciary relationship, any insured mortgages held in the fiduciary estate shall be transferred to a mortgagee approved under this section and the fiduciary relationship must be such as to permit such transfer.

(e) Authorized agents. A mortgagee approved under this section may, with the approval of the Secretary, designate an

affiliate or subsidiary of the mortgagee as authorized agent for the purpose of submitting applications for mortgage insurance in its name and on its behalf.

[58 FR 13537, March 12, 1993]

§ 202.14 Nonsupervised mortgagees

(a) Definition. A nonsupervised mortgagee is a financial institution that has as its principal activity the lending or investment of funds in real estate mortgages, and which is not approved under § 202.13, § 202.15, § 202.16, or § 202.17 of this chapter.

(b) General functions. A nonsupervised mortgagee may submit application for the insurance of mortgages and may purchase, hold, service or sell insured mortgages.

(c) Special requirements. In addition to the general approval requirements in § 202.12, a nonsupervised mortgagee shall meet the following requirements:

(1) Except for multifamily mortgagees, it shall have and maintain a warehouse line of credit or other mortgage funding program acceptable to the Secretary which is adequate to fund the mortgagee's average 60 day origination production pipeline, but not less than a $1,000,000 warehouse line of credit or funding program.

(2) It shall file an audit report with the Secretary within 90 days of the close of its fiscal year (or within an extended time if an extension is granted in the sole discretion of the Secretary), and at such other times as may be requested. Audit report shall be based on audits performed by a Certified Public Accountant, or by an Independent Public Accountant licensed by a regulatory authority of a State or other political subdivision of the United States on or before December 31, 1970, and shall include:

(i) A financial statement in a form acceptable to the Secretary, including a balance sheet and a statement of operations and retained earnings, and analysis of the mortgagee's net

worth, adjusted to reflect only assets acceptable to the Secretary, and an analysis of escrow funds;

(ii) A report on compliance tests prescribed by the Secretary; and

(iii) Such other financial information as the Secretary may require to determine the accuracy and validity of the audit report.

(Approved by the Office of Management and Budget under control 2502-0005)

EXHIBITS C AND K IN SUPPORT OF UNITED'S APPLICATION FOR REHEARING AND BRIEF IN SUPPORT OF APPLICATION FOR REHEARING

EXHIBIT C

U. S. Department of Housing and
Urban Development
Alabama State Office
Southeastern Caribbean Area
Beacon Ridge Tower
Suite 300
Birmingham, Alabama 35209-3144

October 24, 1996

M. Christian Ring
Lightfoot, Franklin & White, L.L.C.
300 Financial Center
505 20th Street North
Birmingham, AL 35203

Dear Mr. King:

Subject: HUD Mortgagee Approval

This responds to the two questions posed in your October 24, 1996 letter to Ms. Martha Andrus, HUD's Director of Single Family Housing.

We have restated your questions prior to providing our response.

1. With the exception of the requirements which specifically apply to FHA-insured loans, do the requirements of 24 C.F.R. §§ 202.12 and 202.14 apply to an approved mortgagee under the provisions of the National Housing Act when it originates non-FHA insured (i.e., "conventional") loans?

Answer: Yes.

2. Do the same requirements under 24 C.F.R. §§ 202.12 and 202.14 apply if the same mortgagee originates the same conventional loans, but in a geographic area that has not been designated under 24 C.F.R. § 202.11(a)(4) or approved under 24 C.F.R. § 202.12 (m)?

Answer: Yes

Please advise if additional information is needed.

Sincerely,

/s/_____
Martha K. Andrus
Director
Single Family Housing Division

EXHIBIT K

KIRKPATRICK & LOCKHART LLP

1800 MASSACHUSETTS AVENUE, N.W.
2ND FLOOR
WASHINGTON, D.C. 20036-1800

TELEPHONE (202) 778-9000
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October 25, 1996

VIA TELECOPY AND HAND CARRIED
Mr. Lynn Herbert
Acting Deputy Director
Office of Lender Activities
and Program Compliance
U.S. Department of Housing
and Urban Development
490 L'Enfant Plaza East
Room #3214
Washington. D.C. 20004

RE: United Companies
Lending Corporation

Mortgagee Identification
#74348-0000-3

Dear Mr. Herbert:

Based on our conversation, it is our understanding that, according to the U.S. Department of Housing and Urban Development ("HUD" or the "Department") records, United Companies Lending Corporation "UCLC" is an approved mortgagee under the National Housing Act. UCLC is active

under the Department's records as a HUD-approved mortgagee and has filed the requisite yearly verification report and audited financial reports necessary to maintain compliance with HUD requirements for approved mortgagees.

We understand that UCLC's status as an approved mortgagee is not determined or affected in any way on the basis of whether UCLC maintains a registered branch in any particular HUD field office jurisdiction. We further understand that there are no additional requirements beyond those required of UCLC's corporate office for a branch office to become registered with the Department.

Please contact me at (202) 778-9202 should you find that our understanding of UCLC's approved mortgagee status is inconsistent with that of the Department. Otherwise, please confirm our understanding by executing the acknowledgement below.

Sincerely
/s/_____
Stacey Riggin
Regulatory Compliance

This is to acknowledge that the above understanding is correct in all respects:

Dated this 25th day of October, 1996.

/s/_____
Lynn E. Herbert, Acting Deputy Director
U.S. Department of Housing and Urban Development
Office of Lender Activities and Program Compliance

Supreme Court, U.S.
FILED
MAR 25 1997
CLERK

No. 96-1411

In The

Supreme Court of the United States

October Term, 1996

UNITED COMPANIES LENDING CORPORATION,

Petitioner,

vs.

MICHAEL McGEHEE and JOYCE McGEHEE,

Respondents.

On Petition for Writ of Certiorari to the Alabama Supreme Court

RESPONDENTS' BRIEF IN OPPOSITION

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QUESTION PRESENTED

Whether certiorari review of the Alabama Supreme Court's judgment is proper where: (a) the Alabama Supreme Court's decision is based on independent and adequate state grounds and (b) no federal question is presented?

TABLE OF CONTENTS

	Page
Question Presented	i
Table of Contents	ii
Table of Citations	iii
Statement of Jurisdiction	1
Statement of the Case	1
Summary of Argument	3
Reasons for Denying the Writ	3
I. The Alabama Supreme Court Based Its Decision On Independent and Adequate State Grounds.	3
II. There Is No Federal Question Presented Because The Issue Before The Alabama Supreme Court Involved Construction Of An Alabama Statute.	6
III. The Alabama Supreme Court Correctly Interpreted The HUD Regulations In The Context Of The Alabama Mini-Code Exemption Found In Alabama Code § 5-19-31(a).	8
Conclusion	13

Contents

Page

TABLE OF CITATIONS

Cases Cited:

Fox Film Corp. v. Muller, 296 U.S. 207 (1935) 6

Herb v Pitcairn, 324 U.S. 117 (1945) 5, 6

Klinger v. Missouri, 13 Wall. 257 (1871) 6

Statutes:

Alabama Code §§ 5-19-1, *et seq.* 1

Alabama Code § 5-19-4(g) 1, 2, 11

Alabama Code § 5-19-31(a) 2, 3, 4, 5, 6, 7, 8, 12

28 U.S.C. § 1257(a) 1

Rule Cited:

Supreme Court Rule 10 ..... 1, 8

Other Authorities Cited:

24 C.F.R. § 202.11(a)(4) 10

24 C.F.R. § 202.12 11

24 C.F.R. § 202.12(j) 13

Contents

	Page
24 C.F.R. § 202.12(k)	9
24 C.F.R. § 202.12(m)	9, 10
24 C.F.R. § 202.12(r)	13
61 Fed. Reg. 36, 452 (1996)	9

APPENDIX

Appendix A — Page VI of UCLC's Brief Filed September 21, 1995 in the Alabama Supreme Court 1a

Appendix B — Page 4 of UCLC's May 24, 1995 Petition for Permission to Appeal from the Trial Court's Interlocutory Order Filed by UCLC in Alabama Supreme Court 2a

Appendix C — Document No. 72 Produced by UCLC During Discovery 3a

STATEMENT OF JURISDICTION

The United States Supreme Court cannot properly exercise jurisdiction over this case pursuant to 28 U.S.C. § 1257(a). In addition, no ground exists for granting the Petition under Rule 10 of the United States Supreme Court Rules.

STATEMENT OF THE CASE

On June 21, 1991, Respondents Michael McGehee and Joyce McGehee ("the McGehees") entered into a consumer mortgage loan with United Companies Lending Corporation ("UCLC"). UCLC makes only conventional (*i.e.*, non-HUD) loans and targets borrowers with credit problems. UCLC charged the McGehees 8% for non-refundable pre-paid finance charges or "points".

Alabama has a consumer protection law (*i.e.*, Alabama Code § 5-19-4(g)) which caps at 5% the amount of "points" that a lender may charge in a consumer mortgage loan.[1] Alabama Code § 5-19-4(g) states in pertinent part as follows:

> (g) Notwithstanding the provisions of this or any other section of this chapter, a creditor may, pursuant to a contract, in a consumer loan or consumer credit sale secured by an interest in real property, charge and collect points in an amount not to exceed five percent of the original principal balance in the case of a closed-end loan or credit sale, or five percent of the total line of credit in the case of an open-end credit plan . . .

---

1. Alabama Code §§ 5-19-1, *et seq.* is commonly referred to collectively as the Alabama "Mini-Code".

(App. to UCLC's Petition, E-1). It is undisputed that UCLC's President and legal compliance officer knew about the 5% cap on points well before the McGehee loan was closed. (C. 1398, 937, 1446, 1260, 1262-66, 1279, 1281-82, 1432).[2]

The McGehees filed a lawsuit in the Circuit Court of Mobile County, Alabama against UCLC for violating Alabama Code § 5-19-4(g) (*i.e.*, the 5% points cap). UCLC moved for summary judgment on the theory that UCLC is "exempt" from Alabama's points capping statute by virtue of an alleged Alabama state law "exemption" contained in Alabama Code § 5-19-31(a). The McGehees cross-moved for partial summary judgment on UCLC's "exemption" defense. The Alabama statute which UCLC relied upon, Alabama Code § 5-19-31(a), states in pertinent part as follows:

> (a) The provisions of this chapter [i.e., of the Alabama Mini-Code]. . . shall not apply to any loan, forbearance, credit sale, lease, or other transaction involving an interest in real property, where the creditor is a lending institution which is an approved mortgagee under the provisions of the National Housing Act or is exempt from licensing under this chapter. . . .

(App. to UCLC's Petition, E-1).

The trial court held that UCLC is not "exempt" under § 5-19-31(a) of the Alabama Code. The trial court denied UCLC's summary judgment motion and granted the McGehees' partial summary judgment motion. The Alabama Supreme Court affirmed the trial court and held that UCLC is not "exempt" from Alabama's points capping statute. Specifically, the Alabama

2. References to the clerk's record will be made with a "C" followed by the appropriate page number.

Supreme Court, construing an Alabama statute, held that UCLC is not an "approved National Housing Act mortgagee" under Alabama Code § 5-19-31(a) with regard to its operations in Alabama.

UCLC now argues that the Alabama Supreme Court "misinterpreted" the Alabama state law "exemption" (*i.e.*, Alabama Code § 5-19-31(a)).

SUMMARY OF ARGUMENT

The Petition for Writ of Certiorari must be denied because: (1) the Alabama Supreme Court's decision rests on independent and adequate state grounds; (2) there is no federal question presented; and (3) the Alabama Supreme Court correctly interpreted the HUD regulations in the context of the Alabama Mini-Code exemption found in Alabama Code § 5-19-31(a).

REASONS FOR DENYING THE WRIT

I.

THE ALABAMA SUPREME COURT BASED ITS DECISION ON INDEPENDENT AND ADEQUATE STATE GROUNDS.

UCLC concedes that "when a state court's construction of a state statute is based on state law, its construction is conclusive . . .", and that state court interpretations of state statutes are generally immune from review by the United States Supreme Court. (UCLC's Petition, pp. 13-14). However, UCLC argues that the Alabama Supreme Court's decision is "completely based" upon Federal law. (Petition, pp. 8, 13-15). UCLC is wrong.

The Alabama Supreme Court construed *an Alabama statute* (*i.e.*, Alabama Code § 5-19-31(a)) and held that UCLC is not an "approved mortgagee under the provisions of the National Housing Act" with regard to its operations in Alabama. In so holding, the Alabama Supreme Court relied upon the following principles *of Alabama law*: (1) the Alabama Mini-Code was enacted for consumer protection and should be construed to effect that purpose; (2) the Alabama Mini-Code was intended to protect the public by regulating creditors and public benefit statutes must be construed most favorably to the public; and (3) the Alabama law requires that exemptions to a statutory scheme should be strictly construed against the party seeking benefit of the exemption (*i.e.*, UCLC).

Specifically, the Alabama Supreme Court held as follows:

> The Mini-Code was enacted for consumer protection and so should be construed to effectuate that purpose, see, e.g., *Jackson v. CIT Group/Sales Financing, Inc.*, 630 So. 2d 368 (Ala. 1993); *Spears v. Colonial Bank of Alabama*, 514 So. 2d 814 (Ala. 1987); *Edwards v. Alabama Farm Bureau Mut. Cas. Ins. Co.*, 509 So. 2d 232 (Ala. Civ. App. 1986), *cert. quashed*, 509 So. 2d 241 (Ala. 1987); *Derico v. Duncan*, 410 So. 2d 27 (Ala. 1982).
>
> Because the Mini-Code was intended to provide protection to the public by regulating creditors, it should be construed so as to effectuate that public protection. "Statutes intended for the public benefit are to be construed most favorably to the public." *St. Paul Fire & Marine Ins. Co. v. Elliott*, 545

> So. 2d 760, 762 (Ala. 1989); *First Alabama Bank of Dothan v. Renfro*, 452 So. 2d 464, 467 (Ala. 1984); *Gant v. Warr*, 286 Ala. 387, 391, 240 So. 2d 353, 355 (1970); *Employers Ins. Co. v. Johnston*, 238 Ala. 26, 32, 189 So. 58, 63 (1939).
>
> Furthermore, § 5-19-31(a) provides an exemption from the provisions of the Mini-Code and so should be construed strictly against the party seeking the exemption. Exceptions or provisos, which restrict the operation of a statute, "should be strictly construed, and . . . only those subjects expressly restricted should be freed from the operation of the statute," *Pace v. Armstrong World Industries, Inc.*, 578 So. 2d 281, 284 (Ala. 1991).
>
> These principles [i.e., of Alabama law] favor extending the protection of § 5-19-4(g) to an Alabama mortgagor whose Alabama mortgagee is not regulated under the NHA approval procedures and limiting the exemption in § 5-19-31(a) to mortgagees approved to make NHA loans in Alabama.

(App. to UCLC's Petition, C-16).

Any one of the above three state law grounds is sufficient to support the Alabama Supreme Court's construction of the Alabama "exemption" statute (*i.e.*, Alabama Code § 5-19-31(a)). Since the Alabama Supreme Court's decision is based on independent and adequate state grounds, the Petition for Writ of Certiorari must be denied. *Herb v. Pitcairn*, 324 U.S. 117,

125-26 (1945); *Fox Film Corp. v. Muller*, 296 U.S. 207, 210 (1935); *Klinger v. Missouri*, 13 Wall. 257, 263 (1871).

II.

THERE IS NO FEDERAL QUESTION PRESENTED BECAUSE THE ISSUE BEFORE THE ALABAMA SUPREME COURT INVOLVED CONSTRUCTION OF AN ALABAMA STATUTE.

The question before the Alabama Supreme Court was one of state law — *i.e.*, whether UCLC is "exempt" from application of Alabama's 5% points capping law under Alabama Code § 5-19-31(a). The Alabama Supreme Court framed the issue presented to it as follows:

> Pursuant to Rule 5, Ala. R. App. P., this Court granted defendant United Companies Lending Corporation ("UCLC") permission to appeal from an interlocutory order denying its motion for a summary judgment and entering a partial summary judgment for the plaintiffs, Michael and Joyce McGehee. By entering the partial summary judgment, the circuit court disallowed UCLC's defense by which it seeks to establish that § 5-19-31(a), Ala. Code 1975, exempts it from the consumer protection provisions known as the Mini-Code, § 5-19-1 to - 31, Ala. Code 1975 — in particular, the 5% limit on discount points imposed by § 5-19-4(g). *The issue, as narrowed on rehearing, is whether a mortgagee that is not approved to make National Housing Act loans in Alabama comes within the provision of § 5-19-31(a)*

> *that "The provisions of this chapter . . . shall not apply to any loan . . . involving an interest in real property . . . where the creditor is a lending institution which is an approved mortgagee under the provisions of the National Housing Act".*

(App. to UCLC's Petition, C-1 to C-2) (emphasis added).

Clearly, the question of whether UCLC was "an approved mortgagee" under Alabama Code § 5-19-31(a) is one of Alabama state law and involved construction of an Alabama statute. UCLC acknowledged in prior briefs that the issue before the Alabama Supreme Court was one of statutory construction of an Alabama law. In UCLC's September 21, 1995 Brief to the Alabama Supreme Court UCLC stated that this case "involves a question of first impression for this Court [*i.e.*, the Alabama Supreme Court] *about the construction of Section 5-19-31 of the Mini-Code.*" (App. 1a) (emphasis added). And, in UCLC's Petition for Permission to Appeal from the trial court's interlocutory order (*i.e.*, filed by UCLC in the Alabama Supreme Court on May 24, 1995) UCLC represented to the Alabama Supreme Court that "[t]he issue before the Court [*i.e.*, the Alabama Supreme Court] is strictly one of statutory construction." (App. 2a).

UCLC knows that the question before the Alabama Supreme Court was an Alabama state law question. Indeed, UCLC represented to the Alabama Supreme Court that the "controlling" question is one of Alabama state law — *i.e.*, whether UCLC was exempt from Alabama's points capping law under Alabama Code § 5-19-31(a):

II. *THE CONTROLLING QUESTION OF LAW*

This petition involves the following controlling question of law:

> Does *Alabama Code* § 5-19-31 exempt "any" mortgage loan made by a National Housing Act mortgagee from the operation of *Alabama Code* § 5-19-4(g), or only a loan which is actually made under one of the insured programs outlined in the National Housing Act?

(App. 2a).

UCLC's representation to the United States Supreme Court that an important federal question is presented is contrary both to the record and to the representations UCLC made to the Alabama Supreme Court in prior briefs. There is no controlling federal question presented, and no statement by UCLC can alter this fact. Thus, the Petition for Writ of Certiorari must be denied. Sup. Ct. R. 10.

III.

THE ALABAMA SUPREME COURT CORRECTLY INTERPRETED THE HUD REGULATIONS IN THE CONTEXT OF THE ALABAMA MINI-CODE EXEMPTION FOUND IN ALABAMA CODE § 5-19-31(a).

UCLC argues that the Alabama Supreme Court "misinterpreted" the HUD regulations relating to mortgagee approval. UCLC is wrong. In fact, even a cursory examination of UCLC's argument reveals that its argument is misleading.

Prior to a 1996 HUD amendment to 24 C.F.R. § 202.12(m), HUD required that each UCLC branch receive separate HUD approval and that an annual fee for each approved branch had to be paid. (24 C.F.R. §§ 202.12(k) and (m) and C. 852). UCLC has *never* had separate branch approval for the branch where the McGehee loan was closed or for any of its other branches in Alabama. This fact is undisputed. (C. 240, 246, 1210, 1018, 1030, 602-03, 618, 633, 640, 372, 455, 657-58).

The Alabama Supreme Court, applying the rules of statutory construction to the Alabama Mini-Code exemption, and after reviewing the HUD regulations *in effect in 1991* when the McGehees' transaction occurred, found that UCLC was not entitled to an exemption from Alabama's Mini-Code on the theory it was an "approved mortgagee" for purposes of its Alabama operations because it did not have *any* branch approval for *any* of its Alabama offices. (App. to UCLC's Petition, C-7 to C-17).

UCLC relies very heavily, if not exclusively, upon a 1996 HUD rule change which amended 24 C.F.R. § 202.12(m), the HUD regulation which formerly required separate branch office approval. (Petition, pp. 6-7, n.4). In reality, the 1996 rule change actually *supports* the Alabama Supreme Court's conclusion that UCLC was not an "approved mortgagee" with respect to the McGehee loan.

The effective date of the rule change is *August 9, 1996.* 61 Fed. Reg. 36, 452 (1996). The McGehee loan was closed *in June, 1991.* (C. 601-605, 1203, 1336, 1386). Thus, the aforesaid rule change occurred over five years *after* the McGehee loan was closed! This fact is very significant and is perhaps the most compelling evidence that the Alabama Supreme Court correctly concluded that the applicable HUD regulations required separate branch office approval at the time of the McGehee loan. Indeed,

this rule change demonstrates that prior to August 9, 1996 (*i.e.*, the effective date of the rule change), 24 C.F.R. § 202.12(m) *mandated* separate branch office approval, which is precisely how the Alabama Supreme Court interpreted § 202.12(m) of the HUD regulations.

The following four items, although not exhaustive, are other very significant reasons which UCLC conveniently ignores which provide overwhelming support for the Alabama Supreme Court's conclusion that UCLC was not an "approved National Housing Act mortgagee" in 1991 — *i.e.*, the year of the McGehees' loan — with regard to UCLC's operations in Alabama.

First, UCLC's corporate Rule 30(b)(6) representative acknowledged that branch approval from HUD was required for UCLC to be approved to originate FHA/HUD loans from that branch. (C. 852). As the Alabama Supreme Court recognized in its Opinion, UCLC stipulated that UCLC had no HUD approved Alabama branch offices. (App. to UCLC's Petition, C-10). In addition, it is undisputed that UCLC did not obtain separate approval from HUD to originate HUD loans out of UCLC's Mobile, Alabama branch where the McGehee loan was closed. (C. 246, 1210, 1018, 1030, 602-03, 618, 633, 640, 372, 455, 657-58).

Second, the application which UCLC relied upon as support for its "approved HUD mortgagee" theory clearly and expressly states that UCLC's approval was limited to the "HUD Field Office jurisdiction of New Orleans, La." (C. 240). Under 24 C.F.R. § 202.11(a)(4), a mortgagee's approval can be restricted to the geographic area designated by the Secretary of HUD. Thus, UCLC's "approval" was limited by HUD to the HUD field office jurisdiction of *New Orleans*. (C. 240). The McGehee loan was applied for and closed through UCLC's *Mobile* branch office. (C. 246, 1210, 1018, 1030).

Third, it is undisputed that UCLC has *never* in its entire corporate history originated an FHA, VA or HUD insured loan, and it is undisputed that none of the loans originated by UCLC in its entire corporate history are insured by any agency of the Federal government. (C. 803-04, 811-14, 833, 845-46, 1274-75, 1092, 1098, 1100, 1102, 1204, 1604, 1493). In addition, the McGehee loan is *not* an FHA, VA or HUD loan on which UCLC was a National Housing Act mortgagee, and the McGehee loan is not insured by the Secretary of HUD or any other officer or agency of the Federal government. (C. 671-674, 1029, 1093, 1096-97, 1493).[3]

Fourth, documents relating to the McGehee loan transaction further demonstrated to the Alabama Supreme Court that UCLC knew the McGehee loan was in fact subject to the Alabama Mini-Code, including the 5% points cap. During discovery UCLC was forced to produce document no. 72, which is a "screen dump" of computer-stored information about the McGehees' loan with UCLC. That document from UCLC's own computer contains an admission that the McGehee loan was in fact subject to the Mini-Code, *i.e.*, including the 5% cap on points contained in Alabama Code § 5-19-4(g). That document states in pertinent part: "AL MINICODE Y = Yes". (App. 3a).

UCLC proclaims that the "stability and integrity" of the secondary mortgage loan market is threatened by the Alabama Supreme Court's allegedly "unforeseen" decision. UCLC's argument is nothing more than a patently ridiculous scare tactic.

3. The whole purpose behind obtaining HUD mortgagee approval is to allow a lender to participate in mortgage insurance programs authorized by the National Housing Act. 24 C.F.R. § 202.12. Indeed, UCLC's Rule 30(b)(6) corporate representative testified that the reason a lender obtains National Housing Act mortgagee approval is to be able to "originate, process, [and] close insured FHA mortgages." (C. 811). UCLC can make all of the conventional loans (*i.e.*, non-HUD) loans it now makes without National Housing Act mortgagee approval. (C. 814, 846, 1274-75).

The sky will not fall, nor will the secondary mortgage loan market collapse, because of this case.

There is no support in the record for UCLC's "chicken little" argument. (*See* C. 1-1515). Indeed, there is no evidence that this case will have any impact whatsoever on any creditor besides UCLC. (*See* C. 1-1515). There is no evidence that any other lender attempted to create a sham "HUD approved lender" exemption in order to circumvent Alabama's consumer protection laws. And, counsel for the McGehees is aware of no other lender, other than UCLC, that perpetrated this type of deception. UCLC's scare tactics have no support in the record.

Moreover, there is no support in the record for UCLC's argument that the Alabama Supreme Court's decision was "unforeseen". UCLC implies to the United States Supreme Court that UCLC has relied for years upon an official construction of the Alabama exemption statute (*i.e.*, § 5-19-31(a)) which is contrary to the Alabama Supreme Court's decision. Nothing could be farther from the truth. UCLC has not produced any correspondence from HUD (or from anywhere else for that matter) which states that, based on the following undisputed facts, UCLC is exempt from Alabama's point capping statute because it is a bona fide "approved" HUD lender within the meaning of § 5-19-31(a): From its inception as a corporation, UCLC never ever intended to make a single HUD loan; UCLC in fact has never made a HUD loan in its entire corporate history; none of the loans originated by UCLC in its entire corporate history are or were insured by any agency of the Federal government; the McGehee loan is not an FHA, VA, or HUD loan on which UCLC was a National Housing Act lender; UCLC has not complied with the federal regulations governing what a lender must satisfy in order to be an approved National Housing Act mortgagee; UCLC's "approval" was limited by HUD to the HUD field office jurisdiction of New Orleans,

Louisiana; UCLC did not have branch approval to originate HUD loans out of its Alabama branches; UCLC does not have a written quality control plan as required by 24 C.F.R. § 202.12(j); and UCLC does not have fidelity bond coverage as required by 24 C.F.R. § 202.12(r) acceptable to the Secretary of HUD or insurance coverage approved by the Secretary that assures the performance of HUD approved mortgagee's responsibilities. (C. 240, 803-04, 830-831, 833, 845-46, 848, 877, 1201-02, 1306, 1274-75, 1092, 1098, 1100, 1102, 1204, 1104, 811-814; *See* C. 1-1515, 671-74, 1029, 1093).

The reason why UCLC has not produced any correspondence wherein the above facts were disclosed to and approved by HUD is because such correspondence does not exist. Had UCLC fully disclosed the true facts, HUD would have reached the same conclusion that the Alabama Supreme Court reached — UCLC is *not* an "approved mortgagee" with regard to its operations in Alabama.

CONCLUSION

For the foregoing reasons, the Petition for Writ of Certiorari must be denied.

Respectfully submitted,

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APPENDIX A — PAGE VI OF UCLC'S BRIEF FILED SEPTEMBER 21, 1995 IN THE ALABAMA SUPREME COURT

STATEMENT OF THE CASE

This appeal affects the ability of residential mortgage lenders to continue to do business in this state. In its order, the trial court has misconstrued a section of Alabama's "Mini-Code" which, if allowed to stand, will result in immediate, irreparable damage to Petitioner/Defendant United Companies Lending Corporation ("UCLC" or "United Companies") and numerous other entities extending credit to Alabama residents. Unless the trial court's order is reversed, the validity of hundreds of millions of dollars worth of mortgage loans will be called into question.

This appeal involves a question of first impression for this Court about the construction of Section 5-19-31 of the Mini-Code.[1] Under this section, mortgage loans by lenders which have obtained mortgagee approval from the Department of Housing and Urban . . .

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1. Although this Court has not previously decided this issue, the United States District Court for the Northern District of Alabama, in *Dorothy Taylor v. United Companies Lending Corporation, et al.*, Civil Action No. CV-94-AR-2321-E, entered summary judgment in favor of UCLC on its exemption defense. The plaintiff appealed that ruling to the United States Court of Appeals for the Eleventh Circuit. After the Eleventh circuit denied the plaintiff's petition for writ of mandamus on other issues, the plaintiff dismissed her appeal.

APPENDIX B — PAGE 4 OF UCLC'S MAY 24, 1995 PETITION FOR PERMISSION TO APPEAL FROM THE TRIAL COURT'S INTERLOCUTORY ORDER FILED BY UCLC IN ALABAMA SUPREME COURT

II. *THE CONTROLLING QUESTION OF LAW*

This petition involves the following controlling question of law:

> Does *Alabama Code* § 5-19-31 exempt "any" mortgage loan made by a National Housing Act mortgagee from the operation of *Alabama Code* § 5-19-4(g), or only a loan which is actually made under one of the insured programs outlined in the National Housing Act?

If the first portion of this question is answered in the affirmative, then the trial court's order is due to be reversed, and this litigation will be concluded.

III. *REASONS WHY PERMISSION TO APPEAL SHOULD BE GRANTED*

A. A Substantial Basis Exists for a Difference of Opinion on the Controlling Question of Law.

The issue before the Court is strictly one of statutory construction. The trial court's order appears on its face to be contrary to the language of the . . .

1386
5803640601

SCREEN 0950 APP NO. 058-798 ACTION

X "X" IF FINAL PAYMENT CALCULATION "X" IF "BOND FOR DEED" LOAN
FINAL LOAN NUMBER 058-036-40601 SELECT 1 1=1ST 2=2ND MORTGAGE
INTEREST NOTE DATE: 62191 FIRST PAYMENT DATE: 80191 TERM: 180 MONTHS

Y Y=WAIVE LOAN FEE $ Y=WAIVE POINTS 8.000% CHARGES: $2972.24
TAX SERVICE FEE 59.50

LIFE INSURANCE TYPE: (SEE <HELP>FOR CODES)
COVERAGE: $
TERM: MONTHS
D.O.B. INS. 1 D.O.B. INS. 2
PLAN S=S/L T=13% F=15% ESCROW (UG) MOS

ESCROWS: $ 691.94
0.15% FILING FEE: $ 52.20

PREMIUM: GROUP LIFE $
ACCID. & HEALTH $
UG / LG $

HH G COVERAGE: Y =YES | AMOUNT $ | TERM YRS | PREMIUM $
TITLE:

M M=MTG S=SIM-COV MTG $ 42000.00 OWNER $ PREMIUM $ 423.50

NTEREST RATE	AL MINICODE	APR	MONTHLY PAYMENT	CASH OUTLAY
14.000%	Y=YES	15.819%	$ 463.45	$ 30616.89

AST PAYMENT	$ 461.03	AMOUNT FINANCED	$ 34800.00
NTEREST	$ 48618.58	TOTAL FINANCE CHARGE	$ 51590.82
OTAL PAYMENTS	$ 83418.58	NOTE AMOUNT	$ 34800.00

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APPENDIX C — DOCUMENT NO. 72 PRODUCED BY UCLC DURING DISCOVERY

Supreme Court, U.S.
FILED
APR 22 1997
CLERK

No. 96-1411

IN THE

Supreme Court Of The United States

OCTOBER TERM, 1996

United Companies Lending Corporation,

Petitioner,

v.

Michael D. McGehee, and Joyce McGehee,

Respondents.

On Petition for a Writ of Certiorari to the Supreme Court of Alabama

PETITIONER'S REPLY MEMORANDUM

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TABLE OF CONTENTS

TABLE OF CONTENTS i

TABLE OF AUTHORITIES ii

I. THE ALABAMA SUPREME COURT'S DECISION IS BASED ON AN INTERPRETATION OF FEDERAL LAW 1

II. THE ALABAMA SUPREME COURT'S DECISION IS NOT BASED ON INDEPENDENT AND ADEQUATE STATE GROUNDS 2

III. THE MCGEHEES MISCONSTRUE THE RECORD AND UNITED'S PRIOR REPRESENTATIONS 4

IV. CONCLUSION 5

TABLE OF AUTHORITIES

CASES **PAGE(S)**

Auer v. Robbins, 117 S. Ct. 905 (1997)..... 2

Michigan v. Long, 463 U.S. 1032 (1983)..... 3

Pennsylvania v. Labron, 116 S. Ct. 2488 (1996)..... 3

PETITIONER'S REPLY MEMORANDUM

I. THE ALABAMA SUPREME COURT'S DECISION IS BASED ON AN INTERPRETATION OF FEDERAL LAW

The McGehees argue in their Brief in Opposition that the Alabama Supreme Court simply interpreted a state statute according to state rules of construction and that there is no federal question at issue. Brief in Opposition ("Op.") at pp. 6-7. However, on the next page, the McGehees concede that the Alabama Supreme Court interpreted federal law in reaching its decision. Op. p. 8-9. They argue that the Alabama Supreme Court **correctly interpreted** the HUD regulations which implement the National Housing Act and **correctly determined** that United is not an "approved mortgagee" under the National Housing Act. This argument necessarily concedes the existence of federal issues in the case and the existence of this Court's jurisdiction.

The McGehees offer four reasons why the Alabama Supreme Court correctly decided that United is not an "approved National Housing Act mortgagee." Op. pp. 10-11. However, these reasons are irrelevant to the issues raised by the Petition for Certiorari. First, not all of these reasons were even relied on by the Alabama Supreme Court in its opinion. Further, by arguing that the court correctly interpreted HUD regulations, the McGehees necessarily concede that the court did in fact interpret federal law and thus that a federal question exists.

The Alabama Supreme Court relied heavily on its own interpretation of the HUD regulations and held that United is not an approved mortgagee under the National Housing Act. This directly contradicts HUD's determination that United is an approved mortgagee under the National Housing Act. *See* Petition for Certiorari, App. G-3 to G-4. Furthermore, the Alabama Supreme Court failed to give any deference to

HUD's determination.[1] This Court has recently reaffirmed the importance of affording deference to federal agency interpretations of statutes and regulations which they are delegated to implement and enforce. *Auer v. Robbins,* 117 S. Ct. 905, 911 (Feb. 19, 1997) (deference given to the Secretary of Labor's interpretation of agency regulations as set forth in an amicus brief.).

The McGehees' claim, that the Alabama Supreme Court correctly interpreted the HUD regulations, highlights the importance of this case. Their assertions invite this Court to determine the proper level of deference that state courts should give to federal agency interpretations of statutes and agency regulations that have been delegated to those federal agencies and to correct errors when the federal regulations have been improperly interpreted by a state court.

II. THE ALABAMA SUPREME COURT'S DECISION IS NOT BASED ON INDEPENDENT AND ADEQUATE STATE GROUNDS

The McGehees argue that the Alabama Supreme Court's decision is based on three independent and adequate state grounds and that this Court has no jurisdiction to hear the Petition for Certiorari. Op. pp. 3-4. They are wrong.

Although the three asserted state law grounds may be proper tools of state statutory construction, they have no bearing on or application to the proper interpretation of fed-

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[1] The McGehees assert that United "relies very heavily, if not exclusively, upon a 1996 rule change" to demonstrate that the Alabama Supreme Court incorrectly interpreted the HUD regulations. Op. p. 9. This is simply incorrect. United's only reference to the 1996 rule change is in a footnote in which United demonstrates that the Alabama Supreme Court's decision is not based on the rule change and that the decision is incorrect under the HUD regulations in effect both before and after the 1996 rule change.

eral regulations determining whether United is an approved mortgagee under the National Housing Act.

Furthermore, when a state court decision appears to rest primarily on federal law, or to be interwoven with it, this Court will presume that the decision is based on federal law. *See Michigan v. Long*, 463 U.S. 1039, 1041 (1983); *see also Pennsylvania v. Labron*, 116 S. Ct. 2485, 2487 (1996). Assuming each or any of the three state law grounds would be adequate or sufficient to support the court's decision, the Alabama Supreme Court's reliance on the federal issues prevents the asserted state law grounds from being independent as well.

The McGehees concede that the Alabama Supreme Court interpreted federal law in reaching its decision. Thus, any claimed state law grounds are not independent even if they might be adequate. A cursory reading of the court's opinion reveals that its decision is at least interwoven with federal law. The court's decision rests on its determination that "because United's Mobile office is not an approved branch office, ... [HUD] requirements do not apply to any offices it has in Alabama." App. C-10. The Alabama Supreme Court did not decide, as a matter of state law, that Ala. Code § 5-19-31(a) does not apply to United regardless of its status as an approved mortgagee as determined by the provisions of the National Housing Act. The Alabama Supreme Court interpreted federal regulations implementing the National Housing Act and held, as a matter of federal law, that United is not an approved mortgagee under those regulations. App. C-17.

Because the Alabama Supreme Court's decision is interwoven with or relies upon federal law, this Court presumes that it is based on federal law. *Michigan v. Long*, 463 U.S. at 1041. A state court may avoid this presumption if it makes clear by a plain statement that federal law is being used only for guidance, and does not compel the result reached. *Id.* There is no such statement.

Accordingly, this Court has jurisdiction to review the Alabama Supreme Court's interpretation of federal law.

III. THE MCGEHEES MISCONSTRUE THE RECORD AND UNITED'S PRIOR REPRESENTATIONS

The McGehees argue that this case involves only state law issues regarding the proper interpretation of a state statute and that United has previously acknowledged this to be the case. Op. pp. 7-8. This misconstrues the record below.

The statute at issue, Ala. Code § 5-19-31(a), incorporates federal regulations defining the term "approved mortgagee." Until the Alabama Supreme Court's opinion on rehearing, the litigation had proceeded on the assumption that United was an "approved mortgagee under the National Housing Act."[2] Thus the only question was whether the exemption in the statute applied to United, a question involving the proper interpretation of state law.

The Alabama Supreme Court created the federal question on rehearing. There, for the first time, the court held that United is not an "approved mortgagee under the National Housing Act" based on its unexpected interpretation of HUD regulations implementing the National Housing Act. App. C-17. Until this ruling was made, United had argued that the plain language of Ala. Code § 5-19-31(a) applied to it based on the fact that it is a HUD approved mortgagee.

United timely petitioned for rehearing and at its first and only opportunity to do so argued to the Alabama Supreme Court that the opinion on rehearing failed to adequately defer to HUD

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[2] The trial court held that "it is undisputed that [United] is an approved mortgagee under the National Housing Act", App. A-6, but nevertheless interpreted § 5-19-31(a) in such a manner that United was not included within its exemption. App. A-6 to A-8. On appeal, the Alabama Supreme Court upheld the trial court's determination that United was an approved mortgagee under the National Housing Act. App. B-3 to B-6.

regulations and interpretations and incorrectly interpreted HUD regulations. United's failure to address these issues previously, when they were not at issue, cannot be held against it now.

CONCLUSION

For all the reasons set forth in the Petition for Certiorari and for those additional reasons contained in this Reply Memorandum, United requests that a writ of certiorari be granted.

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